BREXIT MEANS BREXIT

TOWARDS A NEW RELATIONSHIP WITH THE UK

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Foreword

On 6 October 2016 the Advisory Council on International Affairs (AIV) received a request for an advisory report on what the shape of the Netherlands' future relationship with the United Kingdom (UK) should be following the referendum in the UK on 23 June 2016, in which a majority of 51.9% of the British electorate who voted chose the option of leaving the EU. In its request for advice, the government stated that it was disappointed with the result but that it respected the outcome. The government views the UK as a valued member of the EU and an important European partner for the Netherlands, and has hence consistently sought to keep the United Kingdom within the EU fold.

The request showed that the government believes it prudent at this point to consider what the shape of the Netherlands' future relationship with the UK should be and in this light it asked the AIV the following questions:

1. From the Netherlands' perspective, what should be the key elements of the new bilateral relationship with the United Kingdom?

2. From a Community perspective, what key elements should be part of the EU's new relationship with the United Kingdom?

3. What implications do the elements referred to in the previous two questions have for Dutch interests and the formation of coalitions within Europe?

4. What should the Dutch government's aims be in its bilateral relationship with the UK in the next several years?

The request for advice is attached as Annexe I.

This advisory report is structured as follows. The introduction sets the result of the referendum and the consequences of the UK's withdrawal in a wider perspective and outlines the potentially far-reaching impact on both the UK and the EU27, specifically the Netherlands. It also points out that the UK's economy is closely entwined with that of many EU member states, particularly the Netherlands. In addition, it covers Brexit's resonance for those in other member states who wish to leave the EU in the light of the rise of Eurosceptic parties in Europe and the prospect of important elections in several EU countries.

Chapter I discusses the specifically British context of Brexit and then places it in a wider European context. Chapter II deals with the negotiating process, examining in turn article 50 of the Treaty on European Union (TEU), concerning a country's decision to withdraw from the Union, the negotiations on future relations, a future trading relationship based on a free trade area, and the transitional period.

Chapter III looks at significant elements of the future relationship with the UK, focusing in particular on financial services, external security and development cooperation, internal security, the free movement of workers, education and research, and the fisheries sector. Chapter IV is devoted to a number of selected topics, particularly the impact of Brexit on the EU budget and the multiannual

financial framework (MFF), and the position of the Court of Justice of the European Union (CJEU).

The possible implications of Brexit for the formation of coalitions within the EU are the subject of Chapter V, which looks not only at strengthening existing coalitions but also at aiming to form new ones.

Chapter VI presents a number of conclusions and recommendations based on the analysis in the previous chapters.

The advisory report was prepared by a committee consisting of Ms M. Sie Dhian Ho (chair), Professor C.W.A.M. van Paridon, Dr A. Schout, Professor M.L.L. Segers, Professor L.A.J. Senden, Professor A. van Staden, C.G. Trojan, Ms M.C.B. Visser and N.P. van Zutphen (all from the European Integration Committee) and Dr A.R. Korteweg (Peace and Security Committee). The executive secretary was A.R. Westerink, assisted by H.C. Raaphorst (trainee). C.W.J. Devillers and B. Anker were the civil service liaison officers from the Ministry of Foreign Affairs.

The committee consulted a number of experts, whose names are listed in Annexe III. The AIV is very grateful to them for their contributions.

The AIV adopted this advisory report at its meeting on 3 March 2017.

Introduction

In the referendum on EU membership held on 23 June 2016, 51.9% of the British electorate who voted said that the UK should leave the EU: in other words, they voted for Brexit. Since then, the UK government led by Prime Minister Theresa May has repeatedly emphasised that it will respect British voters' decision ('Brexit means Brexit', as she puts it) and will make preparations for the UK's withdrawal from the EU. The notification required under article 50 of the Treaty on European Union (TEU) before the withdrawal process can get under way is expected in March 2017. The ultimate withdrawal of the UK will have far-reaching consequences, for the UK itself but also for the EU27 and definitely for the Netherlands.

The fact that the UK has been a member of the EU since 1973 means that the economies of the UK and the other EU member states, particularly those in Western Europe, have become closely intertwined. These links – primarily but certainly not exclusively economic in nature – are strong despite a number of opt-outs from the EU acquis which the UK has secured over the years, for example in important policy areas such as Economic and Monetary Union (EMU) and the area of freedom, security and justice (AFSJ).

Apart from strong economic links, close historical, cultural and personal ties exist between the UK and other EU countries, especially the Netherlands.

The economic ties are particularly visible in significant flows of trade in goods and services, integrated financial markets and substantial mutual foreign investment.[1] The personal ties are represented by large numbers of expats. For example, some 3.3 million citizens of the EU27 live, work and/or study in the UK[2] and some 1.2 million UK citizens live in other EU countries.[3] The cultural interconnectedness can be seen, for example, in the English-speaking world's influences on Dutch society and, albeit to a lesser extent, in Dutch cultural influences in Britain. There is also extensive cooperation in numerous fields, including security and justice, foreign policy and defence, education and science, and agriculture and fisheries. Clearly, Brexit will affect the EU – and certainly the Netherlands – in many ways. From that perspective the vote for Brexit is highly regrettable.

Disentangling the UK from the EU, with which it is so tightly intertwined, will undoubtedly prove to be a complex and lengthy process. It should also be noted that although the UK's withdrawal is sui generis, its decision to leave the EU has unmistakably resonated with dissatisfaction with European policy in other EU member states, something that European heads of state and government already acknowledged in June 2016. At that time they resolved to initiate a process of reflection on the EU, a process that began in Bratislava on 16 September 2016.

1 See for example: <https://www.cbs.nl/nl-nl/nieuws/2017/10/meer-goederenhandel-met-verenigd-koninkrijk-in-2016>.

2 Office for National Statistics, Labour Force Survey, population by country of birth, Q4 2015.

3 United Nations, Department of Economic and Social Affairs (2015). Trends in International Migrant Stock: Migrants by Destination and Origin: <http://www.un.org/en/development/desa/population/migration/data/estimates2/estimates15.shtml>.

The UK's withdrawal thus presents the EU27 with the pressing task of making European policy responsive to the needs and wishes of the people of the member states. The aim should be to show EU citizens that their voice can secure democratic change in EU policy where necessary, so that they need not consider the extremely costly option of exiting from the EU – and this certainly applies to countries that also form part of the eurozone and the Schengen area. It is also possible that Brexit will make it easier to take steps towards closer cooperation in certain fields, steps that could help to improve the EU's policy performance and the protection of EU citizens. These might include better joint management of the EU's external borders and enhancement of the Common Foreign and Security Policy (CFSP), as well as social protection.

This advisory report will also address the political and geopolitical consequences for the EU27 of the UK's intention to withdraw from the EU. In line with the questions put to the AIV, these consequences will be discussed both from a Community perspective and from the perspective of the Netherlands as a member state. The analysis will cover the short- and long-term interests of both the EU and the Netherlands, the challenges facing them both, and possible premises and red lines to be adopted in what are expected to be robust political negotiations. Policy fields that will be the subject of intensive political negotiations will include future trade relations, financial services, the fisheries sector, the CFSP and the Common Security and Defence Policy (CSDP), and Justice and Home Affairs (JHA) cooperation. There is a wide gulf between the standpoints of the UK and the EU27 on the budgetary impact of Brexit and the position of the CJEU. The AIV will examine this point in more detail later in the advisory report.

I Brexit in a wider European context

I.1 The British context

The AIV believes it is important to interpret the outcome of the UK referendum not only in a British but also in a wider European context. This is relevant because it is sometimes said that Brexit could have a snowball effect on other member states where sections of the population also favour withdrawal from the EU. France, Italy, Austria and even the Netherlands are mentioned as potentially next in line to leave.[4] However, as indicated above, the AIV regards Brexit primarily as sui generis.

One major difference between the UK and many continental EU countries is that the UK has secured opt-outs, for example from the eurozone and the Schengen agreements. The Netherlands, on the other hand, participates in both these forms of cooperation. Leaving the EU would therefore have much more radical consequences for the Netherlands than for the UK. The Eurobarometer of autumn 2016 reveals that the Dutch, unlike the British, support such participation. 77% of the Dutch support the euro, putting the Netherlands above average when it comes to support for the single currency in the EU (58%) and the eurozone (70%).[5] And a majority (66%) of the Dutch population takes a positive view of immigration from other member states. The corresponding percentage is lower in the UK, where a majority of no less than 58% has a positive attitude to migration within the EU. Remarkably, this figure rose by nine percentage points following the referendum.[6]

Some common trends can be observed in Dutch and British public opinion on European cooperation. It is clear from the Citizens' Outlook Barometer (COB) that the people of the Netherlands view immigration in general as the country's biggest problem.[7] Given the abovementioned support for immigration from within the EU, it may be concluded that this concern must relate to immigrants from non-EU countries. Support for EU membership has not risen above 50% since 2010. Currently 39% of the Dutch are in favour of membership, after a brief rise to 46% in the third quarter of 2016 (shortly after the Brexit referendum). Moreover, the proportion of the population that disagreed with the statement that Dutch EU membership is a good thing was significantly lower, at 20% in the third quarter. In the third quarter of 2016 only 20% likewise agreed that it would be better if the Netherlands left the EU (Nexit) as against 24% in 2015, while 50%

4 Kate Lyons and Gordon Darroch, 'Frexit, Nexit or Oexit? Who will be next to leave the EU', The *Guardian*, 27 June 2016, consulted on 30 November 2016: <https://www.theguardian.com/politics/2016/jun/27/frexit-nexit-or-oexit-who-will-be-next-to-leave-the-eu>.

5 Standard Eurobarometer 86, 'Public opinion in the European Union, First Results', project no. 2016.8131 (autumn 2016), pp. 26-27.

6 Standard Eurobarometer 86, p. 30.

7 Paul Dekker, Josje den Ridder, Pepijn van Houwelingen and Andries van den Broek, Citizens' Outlook Barometer (*Continu Onderzoek Burgerperspectieven)* 2016/4, Netherlands Institute for Social Research (*Sociaal en Cultureel Planbureau*), 30 December 2016, pp. 16-17.

disagreed (43% in 2015).[8] The Netherlands Institute for Social Research also observed that the proportion of the population that believes that The Hague has transferred too much power to Brussels has remained stable around 57% since 2013.[9] This shows dissatisfaction among the Dutch about the extent of European integration, a concern that also came to the fore in the UK at the time of the referendum.

On the basis of the debate preceding the referendum, the referendum result and statements made by members of the UK government and leading Brexiteers, the AIV distinguishes four crucial issues that concern the British about cooperation in the EU. Drawing from one of the prominent Brexit slogans, the four can be summarised as follows: taking back control on migration, on laws, on funds and on trade. These major issues were also key elements in Prime Minister Theresa May's speech on 17 January 2017, when she explained her government's aims going into the withdrawal negotiations ('A plan for Britain'). These aims are set out in more detail in the White Paper published on 2 February 2017, entitled 'The United Kingdom's exit from and new partnership with the European Union'.[10]

First, grievances in the UK are directed at the free movement of EU workers.[11] At the heart of the Leave campaign were claims that there were too many migrants from other EU member states in the UK, that this was depressing wages, that they were taking jobs away from British unemployed people and that they were costing the country a fortune in benefits.[12] Second, Mrs May stated in her speech to the Conservative party conference in October 2016 that, after Britain leaves the EU, 'we will be free to pass our own laws'.[13] Her Plan for Britain of January 2017 stated 'we will not have truly left the European Union if we are not in control of our own laws'.[14] Parliamentary sovereignty is regarded as a fundamental principle of British democracy.[15] The Leave camp has

8 Paul Dekker, Lisanne de Blok, Joep de Hart, Citizens' Outlook Barometer 2016/3, Netherlands Institute for Social Research, 29 September 2016, pp. 25-26.

9 Dekker *et al.*, COB 2016/4, p. 21.0.

10 See: <https://www.gov.uk/government/publications/the-united-kingdoms-exit-from-and-new-partnership-with-the-european-union-white-paper>.

11 James McBride, 'The Debate over Brexit', CFR Backgrounders, 21 October 2016, consulted on 12 January 2017, see: <http://www.cfr.org/united-kingdom/debate-over-brexit/p37747>.

12 See: Gareth Davies, 'Could it all have been avoided? Brexit and Treaty-permitted restrictions on movement of workers', 19 August 2016.

13 Prime Minister Theresa May, 'Theresa May – her full Brexit speech to Conservative conference', the *Independent*, 2 October 2016, consulted on 9 January 2017, see: <http://www.independent.co.uk/news/uk/politics/theresa-may-conference-speech-article-50-brexit-eu-a7341926.html>.

14 Prime Minister's Office and Department for Exiting the European Union, 'The government's negotiating objectives for exiting the EU: PM speech', 17 January 2017, consulted on 1 February 2017, see: <https://www.gov.uk/government/speeches/the-governments-negotiating-objectives-for-exiting-the-eu-pm-speech>.

15 UK Parliament, 'Parliamentary sovereignty', consulted on 12 January 2017, see: <https://www.parliament.uk/about/how/role/sovereignty/>.

strong objections to the supranational powers of EU institutions, especially the Court of Justice. Third, Foreign Secretary Boris Johnson said that Brexit would mean that 'we will be able to take back control of the money that we currently give to Brussels'.[16] Lastly, the UK also wants independent control over international trade, a power that currently is vested exclusively in the European Commission. Dominic Cummings, campaign director of Vote Leave, one of the largest groups lobbying for the UK's withdrawal, said at an early stage that the UK was better able to draft its own trade agreements with third countries than the EU.[17] Mrs May's Plan for Britain argued that a global Britain 'needs to increase significantly its trade with the fastest growing export markets' outside Europe.[18] Later in its advisory report, the AIV will examine the consequences of these four issues for future cooperation in both a bilateral and a Community context.

I.2 The European context

The UK's withdrawal from the EU in due course will have major consequences not only for the UK itself but also for the EU, in both economic and geopolitical terms. In economic terms the EU will lose its second largest economy measured by Gross National Product (GNP), which will substantially reduce the economic dimensions of the Union. Moreover, the UK has always played – and still plays – an important role in strengthening the single market, which the Dutch government views as the EU's most valuable asset.[19] The UK has also always been in favour of a strong common commercial policy. Brexit may therefore have another significant effect by radically altering the balance of votes with regard to the common commercial policy. In future, the Mediterranean countries would be able to form a blocking minority in the EU27.[20] This could affect more protectionist measures, in particular, such as antidumping measures.

The departure of the UK will also mean a sore loss in the field of foreign policy, for one thing because after Brexit France will be the only EU member state to have a permanent seat on the UN Security Council. The UK's exit may also change the balance of power within the CFSP. The impact on the CSDP may also be substantial. For example, the UK's defence expenditure is the highest in the EU (€50 billion in 2015), followed by France (€40 billion) and Germany (€35 billion). Brexit will thus limit the EU's potential to develop

16 Ashley Cowburn, 'Brexit: Boris Johnson dismisses paying EU "large sums" of money in return for market access', the *Independent*, 4 December 2016, consulted on 9 January 2017, see: <http://www.independent.co.uk/news/uk/politics/brexit-latest-news-boris-johnson-davis-davis-dismisses-paying-eu-large-sums-of-money-in-return-for-a7454736.html>.

17 Bagehot, 'An interview with Dominic Cummings', *The Economist*, 21 January 2016, consulted on 9 January 2017, see: <http://www.economist.com/blogs/bagehot/2016/01/out-campaign>.

18 Prime Minister's Office and Department for Exiting the European Union (DExEU), 'The government's negotiating objectives'.

19 See for example: Letter to the House of Representatives of 9 September 2016 on the Netherlands' aims for the informal meeting of the heads of state or government of 27 EU member states in Bratislava, Parliamentary Paper no. 21 501-20, no. 1143.

20 See for example: <http://www.votewatch.eu/blog/france-more-likely-than-germany-to-lead-the-eu-council-after-brexit-voting-records-in-the-council-show/>.

into a military power that is able and willing to perform the entire range of Petersberg tasks.[21]

It is relevant here that these policy fields are run along intergovernmental lines. This means that cooperation in these areas will be able to continue after Brexit, albeit in a different form. The same applies, for example, to defence cooperation and cooperation between intelligence services. Ways of continuing such cooperation are discussed in section III.2.

The outcome of the referendum on 23 June 2016 prompted the political leaders of the EU27 to reflect on the future of the Union. The European Council took its decision to do so on 29 June 2016; the first informal meeting of heads of state and government of the EU27 followed on 16 September 2016 in Bratislava. At the end of March 2017 at a meeting in Rome, this reflection process (the 'Bratislava process') is to culminate in joint conclusions of the European Council on necessary reforms to the Union.

The government set out its aims for the Bratislava process in a letter to the House of Representatives of 9 September 2016.[22] The letter stated that the government attached importance to ensuring that Europe achieves more and protects Europeans better as it works towards the goals it has set itself, particularly on the core issues of migration, security (both internal and external) and the single market. The government takes the view that a better Europe does not automatically mean more Europe; the aim must now be to consolidate and implement measures that have already been agreed.

It is extremely unlikely that it will be possible to bridge – wholly or partly – the economic and/or political divisions between and the highly divergent interests of Northern and Southern Europe, Eastern and Western Europe and for example the four Visegrád countries and a number of other member states, the European Commission and the European Parliament (EP) by the end of March 2017. Reviewing the spectrum of divisions, Jan Rood, a researcher attached to the Netherlands Institute of International Relations 'Clingendael', notes that at the very least it may be concluded that not enough has come of the convergence that was the goal of the integration process (in other words the hope that member states would grow closer together, ideally on a higher level of development). Indeed, if anything a process of divergence has taken place instead, increasing rather than reducing the differences between East and West and between North and South. Elections in Germany and France later this year may well make it more difficult to find swift solutions and to bridge the divisions that exist.[23] The anti-EU message is attracting an ever wider audience in both countries, which for decades have formed a vital

21 T. Palm, 'Consequenties van een Brexit voor het Europees veiligheidsbeleid' [The consequences of Brexit for European defence policy], *Internationale Spectator* 3 – 2016 (vol. 70). The Petersberg tasks are part of the CSDP and include disarmament operations, humanitarian and rescue tasks, military advice and assistance tasks, conflict prevention and peace-keeping tasks, tasks of combat forces in crisis management, including peace-making and post-conflict stabilisation (article 43 TEU).

22 Letter to the House of Representatives of 9 September 2016 on the Netherlands' aims for the informal meeting of the heads of state and government of 27 EU member states in Bratislava, Parliamentary Paper no. 21501-20, no. 1143.

23 J. Rood, 'Meer, minder, anders: de toekomst van de EU27' [More, less, different: the future of the EU27], *Internationale Spectator* 3 – 2016 (vol. 70).

axis of European integration. Even in Germany, with its long history of pro-EU sentiment, Euroscepticism has gained ground in the form of the *Alternative für Deutschland* party (AfD). One reason put forward to explain Euroscepticism of this kind, not only in Germany but in many other member states including the Netherlands, is the fact that in recent decades the EU has focused on achieving the four freedoms within the EU and has paid too little attention to EU citizens' need for protection.[24] The latter includes social and economic protection (against for example unemployment, insecure and temporary employment contracts, and low wages) and protection in terms of security, both internal and external. Here the need is for protection against both terrorism and external threats, from Russia for instance. The refugee crisis and the resulting large-scale irregular immigration flows have contributed to the sense that the EU's internal borders have been abolished without being replaced by properly protective external borders.

It is difficult to predict what the Bratislava process will mean for the future of European integration. However, it seems likely that the process of differentiated integration, a form of cooperation in which not all the member states have the same rights and obligations, will continue and may even be extended further. Some time ago the AIV advised the government to accept differentiated integration as a necessary instrument that enables progress to be made in European cooperation in certain policy areas, and in this connection to take account of the legitimate objections or limitations of certain member states to engaging in closer cooperation.[25] However, the outcome of the UK referendum has shown that adopting differentiated integration does not in itself provide a way of preventing a member state from leaving the EU.

24 See for example the interview with Luuk van Middelaar: <https://www.nrc.nl/nieuws/2016/09/23/europa-moet-leren-bescherming-te-bieden-4389358-a1523114>.

25 AIV advisory report no. 98, 'Differentiated integration: different routes to EU cooperation', The Hague, October 2015.

II The negotiating process

II.1 The article 50 TEU process

Broadly speaking, three phases can be distinguished in the negotiating process: negotiations on the divorce settlement, the future relationship and the transition period. At this point it is unclear whether these negotiations will run in parallel or sequentially. Negotiations will begin once the UK government has invoked article 50 of the Treaty on European Union (TEU), which provides the legal basis for the withdrawal of a member state from the EU. Essentially, the article 50 process concerns the divorce settlement between the UK and the EU27, taking account of their future relationship. These negotiations can last for no more than two years unless the European Council, in agreement with the member state concerned, unanimously decides to extend this period.[26] However, the option of extending the negotiating period would appear to be virtually ruled out because European Parliament elections are due to take place in 2019 and a new MFF will take effect in 2021.

Once article 50 has been invoked, the European Council will determine guidelines for the negotiations. On the basis of these guidelines the Council will draw up a negotiating mandate on the recommendation of the European Commission (in accordance with article 218, paragraph 3 of the Treaty on the Functioning of the European Union (TFEU)). Michel Barnier (former vice-president of the European Commission) will be appointed chief negotiator (in accordance with the decision of the heads of state and government of the EU27). The Commission will conduct the negotiations in close consultation with the Council, and the EP will be kept regularly informed on progress. Didier Seeuws (former head of cabinet for Herman van Rompuy when he was President of the European Council) will lead the Council's task force. Guy Verhofstadt (leader of the ALDE group in the EP) is the EP's coordinator. The UK's negotiating team is led by Foreign Secretary Boris Johnson, with David Davis, Secretary of State for Exiting the European Union, as the chief negotiator and Liam Fox, Secretary of State for International Trade, with responsibility for trade relations with third countries and the World Trade Organization (WTO). Final responsibility for the negotiations, however, emphatically rests with Prime Minister Theresa May.

The separation negotiations will focus on the status and rights of EU citizens resident in the UK and UK citizens living in the EU27, and on the UK's financial obligations. What is referred to as the exit bill includes pension obligations and budgetary commitments for the structural and cohesion funds. In addition, arrangements must be made for the British members of the European institutions and British officials of the institutions, including British diplomats in the European External Action Service (EEAS). Agreement is also required on the relocation of the agencies based in the UK (the European Banking Authority (EBA) and the European Medicines Agency (EMA)), the UK's withdrawal from participation in CFSP missions, Europol and Frontex, border controls, and detaching the

26 Treaty on European Union, article 50, Official Journal of the European Union, vol. 59, 7 June 2016, 2016/C 202/43-44.

UK from international treaties signed by the EU.[27]

Considering these parts of the withdrawal agreement, which will be concluded by the Council on behalf of the EU after approval by the EP,[28] the AIV believes that it is of prime importance for the Netherlands to reach agreement on the status of citizens of the EU27 resident in the UK and vice versa and their acquired rights. The UK's exit bill is also of great importance to the Netherlands given its connection with the 2019 EU budget and the next MFF. The relocation of EU agencies may also be a matter of interest to the Netherlands, as shown by the Dutch candidacy to be the new host country for the EMA.[29] In chapters III and IV the AIV will explain in more detail the other elements it believes to be important to the withdrawal agreement, a transitional agreement and an agreement on the new Community or bilateral relationship with the UK.

Various reports on Brexit raise the question of whether it is possible to reverse the triggering of article 50 TEU at a later stage.[30] It will in any event be impossible to do so once two years have passed since article 50 was invoked, unless a decision has been taken to extend the negotiations, since the UK will then automatically no longer be a member state.[31] Some people take the view that a British U-turn might be legally possible during the two year period of separation negotiations.[32] The UK Supreme Court decided not to refer this question to the CJEU for a preliminary ruling. In the AIV's opinion, anyway, the question is far more of a political than a legal one.

As regards the progress of the negotiations, the AIV believes that it is important for both parties to adopt a reasonable attitude. Section II.3 explains what could be the consequences of a different – perhaps punitive – attitude on the EU's part. Although it is in the Netherlands' interests for the negotiations to proceed in an orderly manner, the AIV would note that the attitude required to ensure this has so far not always been apparent on the part either of the UK or of other EU member states. In the AIV's opinion, it is vital for the government of the Netherlands to take a firm stance, especially on the status of citizens of the EU27 resident in the UK and vice versa and on the size of the exit bill.

27 Miguel Tell Cremades and Petr Novak, 'Brexit and the European Union: General Institutional and Legal Considerations', European Parliament – DG for Internal Policies of the Union – Policy Department for Citizens' Rights and Constitutional Affairs, PE 571.404, January 2017, p. 19.

28 R.A. Wessel, 'De procedure om de Europese Unie te verlaten – een interpretatie van artikel 50 VEU' [The procedure for leaving the European Union – an interpretation of article 50 TEU], SEW Brexit series – no. 1, January 2017.

29 E.I. Schippers and A.G. Koenders, Letter to the President of the House of Representatives of the States General on the Netherlands' candidacy for the European Medicines Agency (EMA), ref.1082538-160317-GMT, 16 January 2017, p. 1.

30 See for example Judy Dempsey, 'Judy Asks: Is Brexit Reversible?', *Carnegie Europe*, 29 June 2016, consulted on 30 November 2016, see: <http://carnegieeurope.eu/strategiceurope/?fa=63955>.

31 Ibid, p. 15.

32 The UK in a Changing Europe, 'Brexit and Beyond', p. 11.

II.2 Future relations

Various writers have outlined possible scenarios for future relations between the EU and the UK. It is important to note, with regard to all such models, that the exact form and substance of future relations will depend on the approach taken by the UK in the negotiations and on the eventual results of the negotiations between the EU27 and the UK. Studies by think tanks or public institutions have reported on as many as eight different models.[33] Some of them are discussed in brief below.

First, the UK could join the European Economic Area (EEA), which includes Norway, Iceland and Liechtenstein, as a way of participating in the EU single market. The UK would first have to accede to the European Free Trade Association (EFTA). To do so, however, the UK would have to permit the free movement of workers and make partial financial contributions to the EU budget. The CJEU would also retain jurisdiction over the UK in the fields where the EU has competence. In addition, the UK would have to continue to implement EU legislation on the single market, but would have no say in shaping the rules.[34] Consequently, this scenario is at odds with the red lines of the British position as outlined by Mrs May and others.

Second, there is what is known as the Swiss model, which provides – via a large number of bilateral treaties (120) – for full access to the EU single market for goods and processed agricultural products and for cooperation in numerous other areas. Here again, the UK would first have to join EFTA. The price for Switzerland's access to the single market has been acceptance of the free movement of persons (albeit with some preferential treatment for Swiss workers following the most recent referendum). In addition, Switzerland must also contribute to the EU budget and is committed to adopting the relevant EU acquis on the single market. This scenario, too, is diametrically opposed to the British position and therefore appears unrealistic.

Third, there is the Turkish model of a customs union, which provides for free movement of goods (except for agricultural goods) but does not require anything in return by way of free movement of persons or a budget contribution. Turkey does have to apply the common external tariff and is not at liberty to conclude trade agreements for itself. However, it can take advantage of the preferential trade agreements concluded by the EU. This model appears not to be an option either, in view of the UK's explicit desire to be able to pursue a trade policy of its own.

The last model to be mentioned is the Continental Partnership, a half-in-half-out model that however will probably not be acceptable to either the UK or the EU27.[35]

33 See for example Bloomberg Intelligence, 'Brexit Special', Bloomberg Briefs, September 2016; HM Government, 'Alternatives to membership: possible models for the United Kingdom outside the European Union', March 2016; J.C. Bollen, G.W. Meijerink and H.A. Rojas-Romagosa, 'Brexit raakt Nederland meer dan meeste EU-landen' [Brexit affects the Netherlands more than most EU countries], CPB Policy Brief 2016/07, June 2016; Miguel Tell Cremades and Petr Novak, 'Brexit and the European Union', op. cit. chapter 4.

34 Michael Emerson, 'Which model for Brexit?', *CEPS Special Report* no. 147, October 2016, p. 3.

35 Jean Pisani-Ferry, Norbert Röttgen, André Sapir, Paul Tucker and Guntram B. Wolff, 'Europe after Brexit: A proposal for a continental partnership', 25 August 2016, p. 2, see: <http://bruegel.org/wp-content/uploads/2016/08/EU-UK-20160829-final-1.pdf>.

In the light of the above, it seems obvious that the UK will finally opt for the broadest possible free trade agreement. The EU's new generation of free trade agreements includes Comprehensive Free Trade Agreements (CFTAs) like those that have been concluded with South Korea and Canada (the Comprehensive Economic and Trade Agreement or CETA). CETA offers the best point of departure for a future trading relationship between the EU and the UK. The EU has also concluded association agreements in the framework of the European Neighbourhood Policy that contain Deep and Comprehensive Free Trade Agreements (DCFTAs): the agreement with Ukraine is an example. It goes farther than CETA, notably when it comes to the approximation of legislation. Elements of deep integration could conceivably be incorporated into a CETA model, to create a CETA-plus model.

An agreement of this kind could involve the following: abolishing internal tariffs, opening markets for public procurement, reciprocal recognition of norms and standards, cooperation in the field of legislation, a level playing field for competition, opening up markets in services, and agreements on, for instance, intellectual property, investment, dispute settlement, employment rights and sustainable development. The breadth and depth of such an agreement would of course be subject to negotiation. The deeper the agreement, the greater the need to ensure that legislation is equivalent. This means, among other things, that an appropriate dispute settlement mechanism would be required. However, like CETA and the agreement with Ukraine, CETA-plus would not provide for CJEU jurisdiction or a contribution to the EU budget. Unlike a customs union, a Free Trade Agreement (FTA) would not impose a common external tariff, thus leaving the UK free to conclude its own trade agreements.

If the UK reaches no agreement whatsoever in the article 50 negotiations, it will fall back on the general WTO regime, i.e. the most favoured nation (MFN) regime which applies to all WTO member countries that do not have a preferential trading agreement with the EU. This would also entail the reintroduction of tariff barriers and customs formalities.

II.3 Possible stance in Brexit negotiations

The stance taken by the Netherlands in the Brexit negotiations will be determined by various factors. In this connection it must be remembered that the negotiations will be conducted on a joint EU basis, which involves finding a common denominator for differing interests.

Naturally, Dutch interests, both economic and political, should carry a lot of weight. However, the AIV takes the view that it is very important for the EU27 to maintain a united front.

The AIV is also of the view that the negotiations should not turn into a punitive expedition against the UK because of its decision to leave. On the other hand, the withdrawal arrangements should not be so favourable as to encourage other countries to consider withdrawing in their turn.

The AIV favours an orderly Brexit, avoiding a cliff edge scenario in which the UK leaves the EU without an agreement, thus triggering an abrupt change of trade rules on the day after Brexit. The UK would then fall back on WTO rules for its trade with the EU, and that would be in the interests of neither the UK nor the Netherlands. As a major exporter of goods to the UK market, the Netherlands must, in the AIV's opinion, ensure that tariff barriers and customs formalities are not reintroduced when the UK actually leaves the EU.

In the AIV's opinion, cherry-picking should be avoided in the negotiations on a possible transition period.

The AIV also believes it would be advisable not to wait too long before beginning parallel negotiations about future relations and a possible transition period.

In the AIV's view, it will be impossible to complete negotiations on future trade relations within the two-year period. Substantive negotiations on this subject will not take place until after the UK has left the EU. For this reason, too, the AIV attaches great importance to a transition period following immediately afterwards. It is relevant to note here that some commentators assume that the transition period will become the definitive or semi-definitive outcome, given the major problems to be expected in completing negotiations on and securing acceptance for a definitive new cooperation treaty.

As regards future trade relations, the AIV is of the opinion that the Netherlands should be open to a free trade agreement that is both broad and deep. In the AIV's view, future relations should not be limited to trade but should also include arrangements for far-reaching continued cooperation in the fields of foreign and security policy, justice and home affairs, and for cooperation on education, research and innovation.

II.4 Future trade relations

The UK's approach
The speech given by Prime Minister Theresa May at Lancaster House on 17 January 2017 shed more light on the UK's approach to future relations between the UK and the EU on trade policy. She left no doubt as to the hard core of her approach: to take back control of Britain's laws, to bring an end to the jurisdiction of the European Court of Justice, to control immigration to Britain from Europe and to be able to negotiate Britain's own trade agreements.[36] In saying this, she ruled out participation in the single market or a customs union from the outset. She also made it clear that the UK is not in favour of a halfway house, by saying 'no' to 'partial membership of the European Union, associate membership, or anything that leaves us half-in half-out'.[37] This can be regarded as a choice in favour of a 'clean Brexit'.

The White Paper of 2 February 2017[38] elaborated the line taken in the Lancaster House speech, but the hard core of Mrs May's speech remained intact. Her aim is a 'comprehensive, bold and ambitious free trade agreement' with the EU, which is to 'allow for the freest possible trade in goods and services between Britain and the EU's member states'. To that end, the EU and the UK should conclude mutually advantageous customs agreements and incorporate 'elements of current single market arrangements', including the freest possible trade in financial services.

36 See: <https://www.gov.uk/government/speeches/the-governments-negotiating-objectives-for-exiting-the-eu-pm-speech>.

37 See: <https://www.gov.uk/government/speeches/the-governments-negotiating-objectives-for-exiting-the-eu-pm-speech>.

38 See: <https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/589191/The_United_Kingdoms_exit_from_and_partnership_with_the_EU_Web.pdf>.

The WTO context
Whatever form a future trade agreement may take, it will undoubtedly infringe the most favoured nation principle and consequently will have to be in accordance with WTO rules. This is possible under article XXIV, paragraph 5 of the General Agreement on Tariffs and Trade (GATT), provided that the trade agreement takes the form of a customs union or a free trade area, or an interim agreement leading to the formation of one or the other, and fulfils the conditions laid down in article XXIV, paragraphs 5 and 8 GATT. An agreement of this kind may not result in higher duties for third countries and must cover 'substantially all the trade' between the parties to the agreement. Any interim agreement should include a plan and schedule for the formation of such a customs union or of such a free trade area within a reasonable length of time.

In the absence of a free trade area or a customs union or an interim agreement leading to one or the other, trade relations between the UK and the EU will be governed by the non-preferential general WTO regime. This is sometimes referred to as the 'WTO scenario' or the 'hard Brexit' model and would entail, for example, the reintroduction of tariff barriers. The AIV regards this scenario as politically undesirable and economically damaging for both the EU and the UK and therefore believes it should be avoided.

A future EU-UK free trade agreement
As stated above, in the AIV's view, the EU's free trade agreement with Canada (CETA) offers the best point of departure for the type of agreement that the UK is aiming for. An FTA must be negotiated and concluded on the basis of articles 207 and 218 TFEU, as from the date on which the UK is a third country. These negotiations will take some time, even if preparatory work takes place parallel to the article 50 negotiations. It took, for example, seven years to negotiate CETA.

Given the approval decisions required, no more than 18 months will be available for the article 50 negotiations.[39] Besides, all attention will be focused initially on the divorce settlement, the key topic of the article 50 procedure. What is more, the EU27 will first want to be clear on the exit bill, especially as regards the UK's financial obligations and EU27 citizens resident in the UK and vice versa.

Even if negotiations on trade relations are conducted in parallel, it will still be impossible to complete them in such a short space of time, quite apart from whether this is possible under the decision-making procedure laid down in article 50 TEU. The AIV therefore assumes that most of the substantive negotiations on a future FTA will take place after the UK has left the EU and will probably last for several years.

Since the basis of the negotiations will be uniform legislation – after all the UK is still implementing the EU acquis as a member state – the process can probably proceed more quickly than it did with CETA. Nevertheless, negotiating a comprehensive free trade agreement similar to CETA will take some doing, particularly because a common denominator will have to be found for the sometimes sharply divergent interests of 27 EU member states. Moreover, such an agreement may take the form of a mixed agreement, because it will probably cover subjects that are also within the competence of the member states, such as certain aspects of investment relations. A mixed agreement must be ratified at national level, as was the case with CETA. An agreement

39 See for example the remarks of the Commission's chief negotiator Michel Barnier at a press conference on 6 December 2016: <http://ec.europa.eu/info/news/introductory-comments-michel-barnier_en>.

on the trade in goods (and other fields where the EU has sole competence) can enter into force more quickly through provisional application.

An interim period
Prime Minister May assumes that agreement can be reached on both the divorce settlement and the future UK-EU relationship by the end of the time allowed for the article 50 procedure. She is fully aware that such an agreement cannot enter into force overnight. To prevent a hiatus, which would in fact mean reverting to the general WTO regime, she is advocating a phased process of implementation, in particular as regards immigration controls, customs, JHA cooperation and the regulatory framework for financial services.

The AIV is of the opinion that this kind of approach may be desirable from the UK's point of view but still involves elements of cherry-picking. The AIV considers that it will be impossible to reach substantive agreement on a comprehensive FTA and at the same time to agree on an interim period. This may be possible – and indeed desirable, certainly from a Dutch perspective – with regard to tariffs, but in the field of services and regulation it will be virtually impossible, and in the eyes of many politically inadvisable, to anticipate the substantive provisions of a future trade agreement. Moreover, in the services sector – especially in financial services – the issue is not simply the legislation but also the practical application of supervisors and regulators. Even in the case of Switzerland, a country with which the EU has some 120 bilateral agreements, they do not cover financial services, with the exception of non-life insurance. Switzerland enjoys free access to the single market for industrial products and processed agricultural products. In return, Switzerland must adopt EU legislation, guarantee the free movement of persons and contribute to the EU budget. Essentially, these are the same conditions as apply to membership of the EEA: conditions which have proved unacceptable to the UK. In this connection, it is relevant that service provision and particularly establishment (Modes 2 and 3 GATS)[40] generally cannot be viewed separately from a certain degree of free movement of natural persons (Mode 4 GATS).

An orderly transition
All this does not alter the fact that there are sound arguments on both sides for arranging a more orderly Brexit without a cliff edge between the UK's withdrawal and the entry into force of a future free trade agreement. A transitional period would thus be the obvious course. This would mean agreeing on a number of interim measures in the framework of the article 50 procedure (in the article 50 decision or the attached Protocol). It should be noted here that an article 50 decision may not include any elements subject to national competence, since they would require ratification at national level.

Under an interim agreement of this kind, it might be possible for tariff-free trade between the UK and the EU27 to continue, while the UK continues to apply the EU's common external tariff. If the UK were simply to continue its membership of the EU customs union on a temporary basis, this would be relatively straightforward, since the interim agreement itself would represent a customs union. However, the UK wants to leave the customs union as it does not wish to be bound by the common external tariff so that it will be free to conclude trade agreements with third countries. But these two requirements – no common external tariff and no internal tariffs – will be irreconcilable until detailed agreements are in place on the country of origin regime.

40 General Agreement on Trade in Services.

Rules of origin are a complex issue which certainly cannot be resolved before the UK actually leaves the EU. Agreements in this field are particularly difficult because the business model of many production sectors, such as the car industry, is based on global value chains.

Temporary continuation of the customs union
In the AIV's opinion, the most obvious solution would be a temporary continuation of the existing customs union for a period of, say, three years. It should be possible to include an interim period for a customs union in the article 50 decision. However, this would seem to be incompatible with the UK's red line about wishing to conclude its own trade agreements. In practical terms, though, it is an illusion to believe that the UK could negotiate and conclude trade agreements and have them enter into force within this time.

First, there will be capacity problems – in terms of both personnel and equipment – affecting both negotiators and customs services. The latter, for example, will have to issue certificates of origin when the UK becomes a third country. It looks as if the number of customs declarations will quadruple, something for which the UK's computer system is not prepared.

Second, the UK will first have to deposit its goods and services schedules and its commitments with the WTO. Even if the schedules and commitments are identical to those of the EU, this process will require time-consuming negotiations within the WTO on adapting tariff quotas. Principal suppliers will also demand compensation in bilateral negotiations. The process will culminate in multilateral negotiations with some 140 WTO members (excluding EU member states) and decision-making by consensus. Since WTO tariff bindings form the basis for all international FTA negotiations, this represents a significant obstacle from the outset.

Third, it is unlikely that third countries will be willing to conclude agreements with the UK while there is no prospect of an EU-UK free trade agreement. As stated earlier, the UK's claim to be able to conclude free trade agreements with third countries (the US, Commonwealth countries) within a very short period of time appears unrealistic. Practically speaking, it will be very difficult to bring about the Global Britain Mrs May advocates, quite apart from the problems referred to above relating to time, capacity and the WTO. The UK's potential trading partners will want to wait and see how the UK's relationship with the EU turns out and to prioritise their own FTA negotiations with the EU, which ultimately has more significant advantages to offer in terms of market access.

Fourth, as a participant in the EU's customs union, the UK would continue to benefit from the EU's numerous FTAs.

Lastly, an interim agreement of this kind would allow time to resolve the problem of the possible reintroduction of a land border between Ireland and Northern Ireland.

The interim period
An interim period of three years, as advocated above, could be used for intensive negotiations on a comprehensive free trade agreement between the EU and the UK. Once concluded, this FTA could be declared provisionally applicable to the part of trade policy that falls within the EU's exclusive competence. These negotiations would also cover the criteria for the country of origin regime after the UK leaves the customs union. At the same time the UK could negotiate with the EU's FTA partners with a view to integrating the mutual advantages into their respective relationships.

The EU, too, would have to negotiate with its FTA partners in order to adapt the agreements to take account of the UK's withdrawal from the customs union. Although the UK would not be able to have any agreements with third countries enter into force during the interim period, there would be nothing to hinder it from opening talks (for example with the US) aimed at an agreement that would enter into force after the withdrawal from the customs union.

A transitional period with tariff-free trade would certainly be in Dutch interests. After Ireland, the Netherlands is the EU member state most closely entwined with the UK in terms of trade.

The costs of a hard Brexit will thus be relatively high for the Netherlands. The Netherlands Bureau for Economic Policy Analysis (CPB) calculates that in the WTO scenario these costs will amount to 1.2% of GDP, i.e. €10 billion, by 2030. Many sectors are highly dependent on exports to the UK: food processing, chemicals, plastics and rubber, electronic equipment, motor vehicles and parts, and metals and minerals. Together these sectors account for 12% of Dutch GDP. The CPB calculates that overall they will suffer production losses amounting to 5%.[41] (See also Annexe II, 'The cost of Brexit to the Netherlands'.)

Conversely, the UK is also highly dependent on exports to the EU (44% of its total exports). As an example, under WTO rules there would have to be a 10% import duty on cars and 16% on lorries. Added to this would be the production chain problems caused by leaving the customs union. In the agricultural sector, the cost of reintroducing customs tariffs could rise to between 70% (meat) and 100% (beet sugar). According to the *Guardian*, a WTO scenario would add €7.6 billion a year to the costs of British exporters.[42]

Technical barriers to trade, norms and standards
Tariff-free trade will not allow full mutual market access without mutual recognition of norms and standards (technical, health, safety, environmental and social).

The question is whether an interim agreement can include mutual recognition of norms and standards as well as tariff-free trade. Otherwise the UK will not have full and free access to EU markets and vice versa. As a matter of fact, this is the regime that applies to Switzerland: tariff-free trade on the basis of a free-trade agreement plus a bilateral agreement with the EU on mutual recognition.

However, there are a number of snags here. First, it is doubtful whether the EU member states are prepared to go this far without concessions from the UK on free movement of workers or a contribution to the EU budget, as in the Swiss model.

Second, it would be difficult to ensure that UK legislation – and its application in practice – remained equivalent throughout the interim period. Continued recognition of the CJEU's jurisdiction is a major issue for the UK (this is discussed in more detail in section IV.2).

41 J.C. Bollen et al., 'Brexit raakt Nederland meer dan meeste EU-landen', CPB Policy Brief 2016/07.

42 See: <https://www.theguardian.com/uk-news/2017/feb/20/no-deal-brexit-would-mean-6bn-in-extra-costs-for-uk-exporters?utm_source=POLITICO.EU&utm_campaign=b1acee4cc3-EMAIL_CAMPAIGN_2017_02_20&utm_medium=email&utm_term=0_10959edeb5-b1acee4cc3-189887225>.

Despite their close links with the EU, Switzerland and Turkey do not acknowledge the jurisdiction of the CJEU, for historical reasons. In fact the Swiss model includes neither efficient monitoring nor an efficient dispute settlement mechanism. Disputes are brought before the various committees appointed under the bilateral treaties.

The EU hopes to change this, in any event by introducing an integrated dispute settlement mechanism based on that of the WTO. A similar arrangement would be possible after the UK leaves the EU, both for an interim period and for the eventual FTA.

UK legislation could be monitored by a joint committee. The options for dispute settlement are an arbitration system along the lines of the WTO Dispute Settlement System or similar models in existing FTAs. Annex A to the UK government's White Paper summarises a number of examples. In the AIV's view, the EU need not request an Investor-State Dispute Settlement (ISDS) mechanism. It would probably be more logical for the UK to be the party to do so.

Services
When it comes to services, the WTO's General Agreement on Trade in Services (GATS) contains a clause similar to the one on goods in GATT but with different wording (article V GATS, entitled 'Economic integration'). This provision renders 'substantially all the trade' as 'substantial sectoral coverage' and makes it impossible to deviate from the MFN principle for any sector such as financial services. Anticipating an FTA is a far less obvious course in the service sector, in both substantive and political terms, than it is in relation to goods. A number of considerations on this point are set out above.

From the UK's point of view, an interim agreement with no transitional arrangement for financial services would be difficult to sell on the home front. The financial sector accounts for 11% of UK GDP. Conversely, the Netherlands' financial sector, among others, is heavily reliant on the City of London. This is discussed in more detail in the next chapter.

For the long term, the UK hopes to achieve the greatest possible freedom for financial services. In the meantime, it wants to maintain the UK's passporting rights in full throughout the transitional period. In the AIV's opinion, this is politically impossible. The EU27 would regard this aim as cherry-picking and as an undesirable anticipation of a future free trade agreement, quite apart from the fact that a number of countries hope to attract jobs to their own financial centres. However, the AIV does take the view that ways should be sought to minimise disruption to the financial system and to facilitate an orderly transition.

Conclusions
In conclusion, the AIV takes the view that future trade policy relations will logically take the form of a comprehensive FTA. The agreement with Canada provides a good basis. Since the UK's legislation is so closely entwined with the EU's, it is highly likely that such an agreement will lead to deeper integration than is the case with CETA. It will take a number of years to negotiate an agreement of this kind, but – given that the starting points of the two parties will be so similar – probably less time than it did to conclude CETA.

It is legitimate to assume that an FTA of this kind will completely abolish customs duties on practically all goods. Whether this will also apply to all agricultural products will depend on the autonomous subsidies policy that the UK will introduce after leaving the EU.

The AIV believes that an interim arrangement will be advisable to facilitate an orderly transition. This interim period should in any event provide for tariff-free trade in goods between the EU and the UK. This will not be feasible unless the UK applies the common external tariff. The AIV therefore advocates continuing the customs union for three years.

The question of whether such an interim arrangement should also cover technical barriers to trade, norms and standards can be negotiated in the framework of the article 50 procedure. In that case the AIV thinks that it will be important to ensure continued equivalence of standards in the UK.

As regards the services sector and the other sections of a future FTA, the AIV believes it is neither possible nor politically advisable to anticipate the substantive provisions of a future free trade agreement. These matters should form part of the FTA negotiations, as should financial services. However, the AIV does take the view that ways should be sought to minimise disruption to the financial system and to facilitate an orderly transition.

III Other elements of the future relationship with the UK

In the future relationship with the UK – both between the EU and the UK and between the Netherlands and the UK – economic, financial and trade interests will be crucial. This chapter takes a closer look at a couple of economic sectors – financial services and fisheries – and the free movement of workers. But there are also other areas where it will be essential in the future to preserve good relations with the UK, both for the EU and bilaterally. This is particularly true with regard to foreign and security policy, internal security, and education and research.

III.1 Financial services

UK position
The financial sector is very important to the UK. It employs more than a million people and accounts for some 11% of UK GDP. The UK is the biggest net exporter of financial services and insurance products and is responsible for some 24% of all financial services within the EU.[43] Moreover, the total assets of foreign banks established in the UK amount to 186% of GNP and those of the UK's own banks to 200% of GNP. International financial institutions establish their head office in London because the EU financial services passport gives them access to EEA markets. Half of the world's largest financial service providers have their European headquarters in the UK. Of the 250 foreign banks in the UK, 170 are from outside the EEA. Passporting rights are important above all to the larger financial institutions, as they conduct the most cross-border business in the EU.

According to the International Monetary Fund (IMF), the UK financial sector owes a substantial portion of its growth to the EU single market. Passporting rights (ensuring the free provision of services) have existed for banks since 1992 and have been steadily expanded, partly in response to G20 commitments on effective oversight of the sector which were made after the financial crisis. As a result London has grown to become one of the three global financial centres alongside Hong Kong and New York. A high concentration of financial service providers, good infrastructure, and the market for talent have turned the sector into an ecosystem for innovation and a FinTech hub.

Falling back on the system of equivalence would engender a great deal of uncertainty for the UK. The principle of equivalence is a means employed in EU financial services legislation to indicate that third countries comply with the EU's legislative and supervisory framework. It does not however apply to everything, and third countries can only request equivalence if this is explicitly provided for in EU legislation. Moreover, equivalence decisions can theoretically be withdrawn by the Commission at any time.[44] These uncertainties make for an unstable basis for ensuring continued access to the EU single market in the future.

43 European Parliament Briefing, 'Brexit: the United Kingdom and EU financial services', 9 December 2016, see: <http://www.europarl.europa.eu/RegData/etudes/BRIE/2016/587384/IPOL_BRI(2016) 587384_EN.pdf>.

44 See: <http://www.europarl.europa.eu/RegData/etudes/BRIE/2016/587369/IPOL_BRI(2016) 587369_EN.pdf>.

In her speech of 17 January 2017, referred to earlier, Prime Minister Theresa May indicated that the UK does not seek complete access to the single market, but is looking for a new, comprehensive and ambitious free trade agreement taking in elements of the single market in certain areas. She explicitly mentioned the freedom to provide cross-border financial services. In this regard she employs the practical argument that it makes no sense to start again from scratch when the UK and the remaining member states have adhered to the same rules for so many years. The UK has implemented the relevant EU legislation and indeed was the architect behind certain concepts underlying, for example, the Bank Recovery and Resolution Directive (BRRD).

The prospect of impending Brexit has already stirred up unrest in the City. Two days after Mrs May's speech, the two biggest European banks, UBS and HSBC, announced that they would be transferring a thousand jobs from London to Frankfurt and Paris in anticipation of the damage that Brexit is expected to cause. Goldman Sachs has said it has not yet reached a decision on relocation. This bank is however setting up a new office in Frankfurt to bring its European operations together. In addition, staff who advise French and Spanish businesses are being moved to those countries, some operations are being relocated to New York, and back office activities are being concentrated in Warsaw.[45]

Europe's biggest bank, HSBC, is starting from a strong position since it already has a large office in Paris that holds most of the licences required by an investment bank. In 2016 UBS set up an office in Frankfurt to concentrate its asset management operations. Lloyd's of London is also considering setting up an office in Frankfurt.

The City of London Corporation is calling for an interim arrangement at the end of the two-year period following invocation of article 50 TEU so that the financial sector could continue to exercise its passporting rights until a completely new relationship is negotiated.[46] It is clear that moving operations away from London will have major financial consequences for the UK.

EU position
There is an extensive framework of rules and regulations that applies to banks, insurance and investments, as well as to investment products and financial infrastructure. Since 2008 there has been further integration or 'deepening', including the 'single rulebook'. Furthermore, rules have been drawn up covering activities that had hitherto not been regulated at EU level or in many cases even at national level, such as rating agencies, hedge funds and derivatives markets. An example is the Markets in Financial Instruments Directive (MiFID), which now regulates price transparency, the use of algorithms and data reporting services.

The size of the UK financial sector is also of great importance to the EU. Seventy-five per cent of profits in the capital market and the banking sector are earned in the UK and 37% of assets under management (AUM) for major clients like pension funds and government authorities in the EU are managed in the UK. The possible consequences of the partial dismantling of the City's ecosystem and the fragmentation and spreading of its activities over a number of European cities were recently mapped out by a number

45 See: <http://uk.reuters.com/article/us-davos-meeting-hsbc-idUKKBN1520SO>.

46 See: <http://fortune.com/2017/01/18/ubs-goldman-sachs-brexit/>.

of experts from the Brussels-based Bruegel think tank.[47] Their study made clear that Frankfurt, Paris, Dublin and Amsterdam were best placed to gain from such a scenario. They estimate that some 30,000 jobs could be shifted from London to the EU27.

If, pending an FTA and in the absence of a transitional arrangement, it proves necessary to fall back on WTO rules, European business will no longer have access to the City's financial services. Schoenmaker (Bruegel) points out that this will make capital more expensive. A number of financial firms say they are already taking action to secure their access to the single market by opening offices in other EU member states.[48] Since a large number of licences are needed and not all member states possess the requisite supervisory expertise, this process may cause problems. The question arises as to whether smaller member states are equipped to provide a stable base for an influx of large financial institutions seeking licences. In the long run this could undermine the stability of the financial system in the EU.

The key question is whether the EU will seek to achieve a situation in which the City's ecosystem (the City being understood to mean the entire financial sector, not the City of London alone) is preserved for European business, or whether EU member states, like France and Germany, will seek to dismantle that ecosystem for the benefit of their own financial services industries.

The AIV takes the view that primary importance should be accorded to minimising the disruption to the financial system within the EU and mitigating the adverse impact of Brexit on the system of financial services to the fullest extent possible. Decisions on third-country regime (TCR) equivalence may offer a fall-back position, but they cannot be applied to all financial services and may be withdrawn by the Commission. They offer the advantage that they can in principle be applied to any third country and hence do not infringe the MFN principle. It is also possible that the scope of equivalence may be widened, making this option even more attractive. This approach would also enable the safeguarding of rights under financial contracts that extend beyond the date on which the UK actually leaves the EU.

The European Commission's Directorate-General for Financial Stability, Financial Services and Capital Markets Union (DG FISMA) launched a new public consultation on 20 January 2017 on the action plan to build a capital markets union. European capital markets are underdeveloped and fragmented. European equity markets are only half the size and bond markets less than a third of the size of those in the United States. Moreover, there are wide disparities between individual member states. Greater integration of capital markets will increase efficiency and will support Europe's financing capacity with a view to growth. Stronger capital markets should complement Europe's tradition of bank financing.

In September 2016 the Commission announced that it would accelerate the deepening of the capital markets union. It is not yet clear how this process should be taken forward without the UK, which currently has by far the biggest capital market in the EU, and whether that should have consequences for the capital market after the UK's departure.

47 See: <http://bruegel.org/wp-content/uploads/2017/02/PC-04-2017-finance-090217-final.pdf>.

48 See: <http://bruegel.org/2017/02/making-the-best-of-brexit-for-the-eu27-financial-system/>.

Brexit may very well provide an extra stimulus to deepen and speed up the integration of the European capital market.

The Netherlands' position
The Dutch financial sector is fearful that the level playing field in the industry may disappear and an offshore entity may emerge off its coast that engages in regulatory competition.

So far the Dutch government and the Dutch Banking Association have not made visible efforts to shift to the Netherlands certain activities currently performed in the UK. Not many are advancing the idea of the Netherlands as an alternative location to London, at least not publicly.

The AIV emphasises the importance of an orderly transition and recognises that the City's hub function is very important to continental banks too. This must be set against the fact that financial services are one element in much broader negotiations. In the first place the Netherlands must give consideration to sectors that depend heavily on exports to the UK.

The AIV believes that a future FTA with the UK must include a sizeable chapter on financial services. Full participation in the single market with passporting rights would seem however not to be an option given that the UK has explicitly ruled out an EEA scenario. Even the City is now working on the assumption that retaining passporting rights in the EU is not a viable proposition in the long run.

The AIV also believes that alternative arrangements can be devised in a CFTA to make the provision of services to and from the UK as free as possible. Equivalence agreements of the kind mentioned above can play an important role in this regard.

III.2 External security – foreign policy and defence

The discussion on the shape of the future relationship between the EU and the UK is primarily focused on trade and financial and economic matters. But there are also other policy areas where continued close cooperation between the two parties is in their mutual interest. One of these areas is foreign policy and defence.

The EU faces wide-ranging external threats: Russian intimidation in Eastern Europe; attacks by terrorist movements and cells based in the Middle East; and hotbeds of instability on Europe's southern fringes. The AIV therefore feels that the EU should endeavour as far as possible to continue to involve the UK in the preparation and implementation of the CFSP and the CSDP.

The UK has an extensive diplomatic network, holds a permanent seat on the UN Security Council, is – alongside France – the most important military power among the member states, and can draw on the largest development budget of all rich countries after the US. In other words, besides the international experience and reputation it adds to the equation, the UK makes a significant contribution to the resources needed to conduct an effective European external policy. The UK's proposed departure from the EU may also diminish the quality of the EEAS. Moreover, on a number of dossiers the UK has been the driving force behind joint action by EU countries. For example, the UK government played an active role in linking EU sanctions to diplomatic pressure in respect of Iran (because of that country's nuclear programme) and Russia (because of the annexation

of Crimea). It was also prominent in devising and implementing the economic sanctions imposed by EU countries on Bashar Al-Assad's regime in Syria. Because of the central role the City fulfils in global financial flows, the effectiveness of European financial sanctions is limited without UK participation.

Moreover, the UK itself has an interest in working closely with EU member states on foreign and security policy. If the UK can achieve agreement within the EU on a subject that is close to British hearts, the EU functions as a diplomatic multiplier. A recent example is Europe's sanctions policy regarding Burma/Myanmar. Without the UK this policy would not have come about and without cooperation in the EU it would not have been effective. The EU also plays an important role in the Balkans, partly at Britain's urging. In addition, the EU is active – more so than NATO – on the continent of Africa, in the form of stabilisation operations, training missions and development aid. It is a continent where the UK also has major economic and security interests.

It is true that, from an EU perspective, the UK has made a markedly less positive contribution to the development of the CSDP. The UK has always adopted a sceptical if not hostile position towards the notion of building an autonomous European defence capacity. The UK government has not wished to call NATO's primacy into question in matters concerning the security interests of European countries. It opposed the idea of setting up an EU military-civilian headquarters for planning and coordinating European stabilisation operations and training missions, arguing that it would duplicate existing NATO structures. The UK also blocked an increase in the budget of the European Defence Agency (EDA). It is therefore hardly surprising to see that the part played by Britain in missions carried out in the context of the CSDP has been particularly modest, with the exception of naval operations conducted by EU countries around the Horn of Africa and in the southern part of the central Mediterranean.

Although the UK's position concerning the organisation of European defence seems uncompromising, the AIV believes that a re-evaluation cannot be ruled out as a consequence of possible developments in US security policy. If the Trump administration ceased to view NATO as a priority and distanced itself from the US's traditional role as guarantor of European security, the UK government would have no choice but to consider alternatives to its transatlantic military cooperation.[49]

What avenues could be explored in the search for cooperative arrangements between the EU and the UK in the policy areas in question? Since the CFSP and the CSDP operate on the basis of intergovernmental cooperation, seeking solutions in this area would seem to be an easier proposition than determining the shape of future trade relations, which involves the EU institutions. After all, intergovernmental cooperation offers greater scope for applying flexible formulas and making informal arrangements. A paper published by an authoritative research institute identifies four possible models of cooperation ranging from less to more integrated options:[50]

49 See Anne Appelbaum, 'Europe needs a new defence pact and Britain could lead it', *Financial Times,* 16 February 2017.

50 Nicole Koenig, 'EU External Action and Brexit: Relaunch and Reconnect' (Berlin: Jacques Delors Institut, 22 November 2016).

1. Strategic partner (loose cooperation and consultation)
2. Norwegian model (regular consultation and alignment, no inclusion in decision-making)
3. 'Norway Plus' (selective inclusion in informal and operational decision-making)
4. 'Foreign Affairs Council Plus' (systematic inclusion in formal decision-making).

The degree to which the UK expresses an interest in staying involved in the CFSP/CSDP will of course be an important consideration for the EU in determining its preferred option. Just as the EU needs to be convinced that working with the UK lends it greater international clout than it would otherwise possess, the UK government needs to realise that linking up with the EU's potential can magnify its own influence. Otherwise the basis for a continued close relationship is absent. Another relevant consideration would seem to be the UK's long-standing aversion to erecting new formal institutions and preference for practical solutions such as informal contact groups. Selective participation in informal and operational decision-making, as outlined above under the 'Norway Plus' model, is compatible with this outlook.

In addition, the AIV takes the view that it is very important to involve the UK in some way in the decisions of the EU's Foreign Affairs Council. Clearly the UK, as a non-member of the EU, cannot participate in the Council's formal decision-making. But ad hoc or permanent observer status, including the right to participate in the Council's deliberations, seems to be a possibility and merits serious consideration. The UK could, by means of separate agreements, comply or not comply with the Council's decisions. The UK could also be given the status of ad hoc or permanent observer on the Political and Security Committee, the body which prepares and implements the CFSP at ambassador level. A condition for such an agreement could be that London may not, for as long as the UK is still a full member of the EU, unilaterally block decisions of the EU27 in the area of the CFSP/CSDP, like the proposed military-civilian planning capability.

Anglo-Dutch bilateral defence cooperation
Outside a formal EU framework, several European countries have concluded bilateral agreements on defence cooperation with the UK. The best known (and probably most important) of these are the Lancaster House treaties between France and the UK signed in 2010. One of these treaties provides for cooperation between the two countries' nuclear forces. The general expectation is that Brexit will not affect these treaties.

The Netherlands also engages in forms of military cooperation with the UK. Since as far back as 1973, Dutch and British marine units have been integrated in an Anglo-Dutch amphibious force, which can in principle be deployed anywhere in the world, in all circumstances and climatic conditions. To date, however, this force has never been actually deployed in a conflict zone. The Netherlands has also committed itself to participating in the Joint Expeditionary Force, which will be built around British military forces and which will also include Norway, Denmark and the Baltic countries. This intervention force is intended to be operational in 2018. The Netherlands and the British have also made agreements on training and exchanging military personnel.

In view of the great importance that should be placed on keeping the UK closely involved in forms of European military cooperation, whether multilateral or bilateral, the AIV takes the view that the Dutch government should continue its current bilateral ties with that country. Military cooperation with the UK should be assessed on its own merits and should not suffer from possible friction between the EU and the UK concerning trade policy.

III.3 Development cooperation

The UK is one of a handful of EU member states that currently spend at least 0.7% of GNP on development cooperation.[51] The UK also makes an important contribution to the EU development cooperation budget. In 2014, for example, the UK allocated €1 billion for the EU development budget (including the Global Europe programme) out of a total of €6.9 billion. In the same year, the UK contributed €0.4 billion to the European Development Fund (EDF) – which does not come under the EU budget – which totalled €3.1 billion. Besides contributing to the EU budget for development cooperation and the EDF, the UK also helps to finance the EU Trust Funds for specific purposes or crises. The Trust Funds also fall outside the EU budget. UK contributions in 2014 accounted for some 14% of the EU development cooperation budget.[52]

Besides the substantial UK financial contributions to the EU development budget, the EU also benefits from extensive British development expertise, especially at the Department for International Development (DFID), and from the prominent role played by British experts and institutions at the EU in the field of development.[53] UK initiatives in response to the Ebola outbreak in West Africa and to the conflict in Syria, when European countries and the EU made substantial contributions at the UK's instigation, demonstrate that the UK also often acts as a catalyst in the area of EU development policy.[54]

As a consequence, Brexit may have an adverse impact not only on the financial resources at the EU's disposal for development cooperation, but also with regard to development expertise and experience.

The UK itself also stands to gain from continuing its close cooperation with the EU on development, as the EU offers the UK channels to amplify the scope and effectiveness of efforts in this field.[55] Brexit could also mean the UK loses an influential position within the world's biggest provider of development assistance – the EU. This is why the White Paper published in early February 2017 emphasises that the UK wishes to carry on working with European and other international partners so that it can continue to tackle global challenges in the future.[56] As regards the possibility of continuing to use the EU channel, it is relevant to note that in the most recent Multilateral Development

51 See: <https://data.oecd.org/oda/net-oda.htm>.

52 See: <https://www.cgdev.org/blog/beyond-brexit-how-will-eu-overseas-development-assistance-be-affected>.

53 See: <http://www.euractiv.com/section/development-policy/opinion/tues-what-would-brexit-mean-for-development>.

54 Koenig, N., 2016, 'EU external action and Brexit': see: <http://www.delorsinstitut.de/2015/wp-content/uploads/2016/11/20161122_BrexitExternalAction-Koenig-JDIB-Nov16.pdf>.

55 See: <https://www.gov.uk/government/speeches/the-governments-negotiating-objectives-for-exiting-the-eu-pm-speech>.

56 'The United Kingdom's exit from and new partnership with the European Union'. See: <https://www.gov.uk/government/publications/the-united-kingdoms-exit-from-and-new-partnership-with-the-european-union-white-paper>.

Review, EU development projects and organisational strength scored well. The Review also emphasised that the UK would continue to contribute to the EDF for the time being.[57]

The Netherlands and the UK are largely of like mind when it comes to development cooperation, such that they often work together closely in both an EU and a UN context. Hence the Netherlands also stands to benefit from continuing this cooperation, partly because the UK is an influential and like-minded partner within the EU in the sphere of development cooperation. For the Netherlands, continuing to work together on European projects and programmes means continuing to work with a partner that is not only like-minded, but is also a leading and expert player in this field. In the AIV's view, this is important for the UK, the Netherlands, the EU and developing countries alike, not least because keeping up mutual coordination and cooperation enhances the effectiveness and scope of development interventions.

The AIV therefore considers it to be very important to maintain current cooperation with the UK on development to the greatest possible extent. The most likely option would seem to be for the UK to continue contributing to the EDF, as this fund falls formally outside the EU budget. Countries' votes within the EDF are weighted in relation to their contribution, a significant factor for the UK as a major donor. This means that control over the expenditure of the fund's resources is related to the financial contribution made by countries to the EDF. This option would therefore seem attractive to the UK, which would thereby retain a measure of control over where and how European development funding is spent. It would also be attractive to the EU and to the Netherlands, because it would enable them to retain the UK as a like-minded partner in the field of development cooperation. Furthermore, the UK's financial resources, expertise and extensive mission network could continue to be used to deliver European development assistance as effectively as possible in the countries and regions where it is needed most.

III.4 Internal security – cooperation in the field of Justice and Home Affairs (JHA)

The Lisbon Treaty put in place a more efficient structure and a more efficient decision-making procedure in the Council for cooperation in the field of JHA. The area of freedom, security and justice (AFSJ) is one in which in which the free movement of persons is ensured in conjunction with appropriate measures with respect to external border controls, asylum, immigration and the prevention and combating of crime (article 3, paragraph 2 TEU).

The UK and Ireland have negotiated opt-outs in the field of JHA cooperation and only participate in the adoption and application of specific measures after an explicit decision to this effect, i.e. an opt-in. One of the UK's opt-ins concerns the Common European Asylum System (CEAS). The UK opted in during the first round of legislation in 2004, but did not do so again in 2013-2014. In the area of combating crime, the UK opted in to the European Arrest Warrant (EAW), which simplifies the procedure for the extradition of suspects between member states.

A number of agencies were established to help implement AFSJ policy, such as Europol for police cooperation, Eurojust for cooperation in criminal cases, and Frontex for EU external border control. The UK performs an active role at several of these agencies, as

57 See: <https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/573900/Multilateral-Development-Review-Dec2016.pdf>.

evidenced for example by Rob Wainwright's directorship of Europol and the number of other British employees at that agency. The UK places great importance on Europol, as is clear from its wish to ratify, by means of an opt-in, the new Europol regulation, which is due to enter into force on 1 May 2017.

Although it has never participated fully in the former JHA and current AFSJ cooperation, the UK does set great store by the continuation of this cooperation, and contributes actively to it not only through the agencies but also for instance by developing policy on police cooperation and access to data with a view to law enforcement. In other fields, such as Schengen cooperation on border controls and visas, which has existed since 1985, the UK secured opt-outs at an early stage. And recently, in 2014, the UK negotiated a large number of opt-outs, followed by a number of opt-ins, relating to crucial aspects of AFSJ cooperation, partly at the urging of the then Home Secretary and current Prime Minister Theresa May.[58]

Elements of AFSJ cooperation in which the UK currently participates include not only Europol and the EAW, but also the Schengen Information System (SIS), the European Criminal Records Information System (ECRIS), Passenger Name Records (PNR), Eurojust, the European Investigation Order and the Victims Directive. Brexit will mean not only that it will be impossible to continue to cooperate in the current manner in the areas mentioned, but also that all British citizens will become third-country nationals from the perspective of EU law from the date on which the UK leaves the EU.

UK position

In her speech on 17 January 2017, Prime Minister Theresa May was very clear on what the UK wanted with regard to future cooperation to combat crime and terrorism. She said among other things, 'And a global Britain will continue to cooperate with its European partners in important areas such as crime, terrorism and foreign affairs.' In fact she intended not just to continue, but also to deepen cooperation: 'With the threats to our common security becoming more serious, our response cannot be to cooperate with one another less, but to work together more.' This should be achieved by means of 'practical arrangements on matters of law enforcement and the sharing of intelligence material with our EU allies'.[59] Mrs May did not comment on what these practical arrangements might look like.

What is clear, however, is that the UK government is seeking a bespoke solution, taking account of what Britain views as its special status and enabling a degree of partnership not permitted to any other non-EU member state. The question is whether this aim is realistic, partly in view of the UK's aims in other areas (trade, access to the single market) where the stakes for the EU and the UK are at least as high if not higher.

A possible stumbling block in achieving agreement in this area is the position of the CJEU. Nick Clegg has set out some of the reasons why this is so:[60]

58 Clegg, N., 'Justice and Home Affairs Cooperation', Fifth Brexit Challenge paper, 15 December 2016.

59 See: <https://www.gov.uk/government/speeches/the-governments-negotiating-objectives-for-exiting-the-eu-pm-speech>.

60 Clegg, N., 'Justice and Home Affairs Cooperation', Fifth Brexit Challenge paper, 15 December 2016.

1. The EU can only act in compliance with the Charter of Fundamental Rights. The CJEU is the ultimate arbiter of this. It is therefore impossible for the EU to sign an agreement with the UK that conflicts with either the Charter or CJEU case law.
2. Second, any agreement needs to be policed. The final agreement between the UK and EU is no exception. It would be open to an EU citizen to take a case to the CJEU and potentially have the EU's decision concluding the agreement annulled.
3. Third, the developing case law of the CJEU is binding on EU member states. To avoid divergence between UK and EU law, the UK would have to continue to respect the rulings of the CJEU.
4. Some form of dispute resolution is necessary in any international agreement. It is difficult to imagine the CJEU not having a role in this regard.

A potential role for the CJEU in future AFSJ cooperation may be difficult if not impossible for the UK to accept. This is patently clear from Mrs May's explicit pronouncements on 17 January 2017. Among other things she said, 'So we will take back control of our laws and bring an end to the jurisdiction of the European Court of Justice in Britain. Leaving the European Union will mean that our laws will be made in Westminster, Edinburgh, Cardiff and Belfast. And those laws will be interpreted by judges not in Luxembourg, but in courts across this country.'[61] In light of this clear statement of position, it will not be easy to reach an agreement on AFSJ cooperation.

EU position
Although as yet there is no formal EU position, in line with the principle of 'no negotiation before notification', it is clear that continuing cooperation with the UK in this area is also highly desirable for the EU27. But from an EU perspective it is similarly unclear as yet how this can be achieved. There are precedents involving non-EU countries that take part in forms of AFSJ cooperation. Cooperation agreements have for example been concluded between Europol and third countries in the form of strategic partnerships (with Russia, Turkey and Ukraine) and operational partnerships (inter alia with Norway, Iceland, Australia and the US). Although the latter form of partnerships goes further than strategic partnerships, it does not allow direct access to the Europol Information System or the Secure Information Exchange Network Application (SIENA). Nor is there any possibility of leading operational projects. This raises the question of how attractive this option would be to the UK.

The SIS is only accessible to Schengen members and countries with special agreements of the kind concluded with the UK, and the European arrest warrant is only available to EU members. The surrender agreement that Norway and Iceland concluded with the EU after 15 years of negotiations is less far-reaching than the EAW and, moreover, has yet to enter into force.

In addition, access to crime data via ECRIS is restricted to EU members. Bilateral agreements do exist with the US, Canada and Australia for the purpose of sharing passenger name records and with the US to share data in the context of the Terrorist Finance Tracking Programme. However, these measures only represent a small part of current AFSJ cooperation.[62]

61 See: <https://www.gov.uk/government/speeches/the-governments-negotiating-objectives-for-exiting-the-eu-pm-speech>.

62 Clegg, N., 'Justice and Home Affairs Cooperation', Fifth Brexit Challenge paper, 15 December 2016.

In light of the foregoing, it is questionable whether, if it were to be possible to reach a bilateral agreement with the UK, such an agreement could go all or part of the way towards achieving the ambitious aims for more intensive JHA cooperation articulated by Prime Minister Theresa May among others.

The Netherlands' position
The AIV is of the opinion that the Netherlands must aim to secure the UK's continued close involvement in JHA cooperation. This is in the interests not only of the UK and the EU27 but also – especially – of the Netherlands. As a neighbouring country the Netherlands works closely – to a greater extent than many other EU member states – with the UK, to combat drug trafficking, serious crime and people smuggling, as well as in other areas. It is relevant to note in this regard that border controls to and from the UK will be tightened up. This will inevitably have an impact on the border control process.

If the UK continues to take part in JHA cooperation in the future, the AIV believes that this should not mean that data exchanged ends up outside an effective and satisfactory system of oversight that meets the requirements of due process and the broader protection of fundamental rights.

A possible way forward
When the UK's membership of the EU ends, this will also spell the end of JHA cooperation with the UK in its current form. An alternative to full membership could be third country participation, as it currently applies for example to Denmark. In that scenario, however, it would no longer be possible to exert influence over the strategic policy of, for instance, Europol. This option would therefore seem to hold little attraction for the UK. The UK will therefore look for a unique future collaborative relationship, which may prove to be an intermediate form between third country participation and full membership.

III.5 Free movement of workers

The free movement of workers is one of the EU's founding principles. Since the rounds of EU enlargement in 2004 and 2007, involving the accession of a number of Central and Eastern European countries whose level of socioeconomic development was considerably lower than the average for EU member states, the free movement of workers has climbed the political agenda. This is because considerably more EU citizens have availed themselves of their right to free movement since that time.

The UK is one of the most popular destinations for these 'EU migrants', as the British call them. The period 1995 to 2015 saw a tripling of the number of immigrants from other EU countries residing in the UK from 0.9 million to 3.3 million. Part of the reason probably lies in the UK's decision, in contrast to most other EU member states, to dispense with a transitional period for the free movement of persons following the 2004 EU enlargement. Net immigration from the EU to the UK was 172,000 in 2015. In that year, 29% of EU immigrants came from Poland. Immigration to the UK has grown considerably over the last 20 years, and a considerable portion of that growth has its origin in other EU countries. Over this period, the share of EU citizens from outside the UK grew from 1.5% to 5.3% of the total population and from 1.8% to 6.3% of the labour

force (people aged over 15 and under 65).[63]

Migration from EU member states has become the subject of increasing controversy in the UK in recent years, stoked by the British media's overwhelmingly negative reporting of the issue. The arrival of large numbers of migrants from Poland and other new member states, it is argued, takes jobs from UK-born workers and depresses their pay levels. EU migrants are portrayed as placing a heavy financial burden on the British welfare state and having a negative impact on local public services like social housing and schools, and on crime figures.

It is clear that, in this highly politicised debate, insufficient distinction is drawn between what can be ascribed respectively to the free movement of persons in the EU, to the UK's political choices (for instance the specific organisation of the UK's social security system and the decision to forego a transitional period for the free movement of workers after the accession of Central and Eastern European countries), and to abuses of free movement, whether deriving from countries of origin or from employers and landlords in the UK. Research by, among others, the London School of Economics[64] has shown that areas of the UK with a high level of EU immigration have not experienced a greater fall in employment or wage levels among UK-born workers, that tax paid by EU immigrants outweighs the cost of social security and public services they receive, and that evidence for the alleged negative social effects is lacking. Downward pressure on pay is largely a result of the financial crisis, weak economic recovery and a low minimum wage. Inequality, inadequate public services and poverty pose a far broader problem in the UK. But a feeling has arisen that EU immigration is a major driving force behind the perceived decline. 'Taking back control over our borders' accordingly became the principal demand of the Leave campaign. It was mainly the unpopularity of EU migration that swayed a majority of British voters to opt for departure from the EU.

The EU27 clearly take a different view of the free movement of workers. The Eurobarometer shows that immigration is also a concern for EU citizens on the continent, but that this mainly relates to immigration from third countries. The free movement of persons within the EU has the support of 79% of EU citizens. In the Netherlands the figure is 77%.[65] Governments of the EU27 have emphasised that the free movement of workers is viewed as an inseparable part of the single market.

UK position

In her Brexit speech, Prime Minister Theresa May said that the UK would stand firm by its demand for control over EU migration. Understanding that the four freedoms are indivisible for the EU, she concluded – as indicated earlier in this advisory report – that the UK must forgo further participation in the single market, and will not for example follow Norway's example, a non-EU country which does participate in it. No clear statements have yet been made concerning how the UK intends to go about regulating

63 J. Wadsworth, S. Dhingra, G. Ottaviano and J. Van Reenen, 'Brexit and the Impact of Immigration on the UK', Centre for Economic Performance Brexit Analysis No. 5, London School of Economics and Political Science, p. 2.

64 Ibid.

65 C. Mortero-Martinez, C. Odendahl, 'What free movement means to Europe and why it matters for Britain', Centre for European Reform, January 2017, p. 5-6.

and limiting migration from EU countries. A system based on work permits, with quotas possibly varying by sector, is often mentioned as a possibility. This will involve making important choices about whether to distinguish between highly skilled and low-skilled jobs, and between migrants from the EU and migrants from third countries. The UK government expects that it will take several years to introduce these new rules. An important question that certainly will arise during the article 50 discussions concerns the rights of the 3.3 million EU migrants living in the UK and the 1.2 million UK citizens who live elsewhere in the EU. Mrs May has indicated that she wishes to prioritise this question.

EU position
Mrs May's own uncompromising conclusion that taking control of 'European migration' to the UK means exiting the single market has for the time being put an end to speculation by some experts about a possible new model in which the UK would continue to take part in the single market but would secure some kind of exceptional position with regard to the free movement of workers. A model of this kind would in any case enjoy little support among the EU27. The EU has always taken a consistent line on the single market and the four freedoms: 'either you're in, or you're out'.

The Netherlands' position
The free movement of workers has also become a political issue in the Netherlands in recent years, albeit less so than in the UK. The principal concerns have centred on claims that workers from other EU member states, in contravention of EU rules, offer their labour in exchange for inferior terms of employment to those applicable in the Netherlands, leading to downward pressure on terms of employment in certain sectors, and to the exploitation of migrants from EU member states. The Dutch government has put these concerns on the political agenda in the EU, calling for 'the same pay for the same work in the same place'. The point is thus emphatically about improving the enforcement of EU rules and being guided by the principle of 'the same pay for the same work in the same place', partly by revising the Posting of Workers Directive, and not about eroding the principle of the free movement of persons or reducing EU migration. The AIV considers it important to draw a sharp distinction between the free movement of workers subject to fair conditions on the one hand, and the UK's rejection of the principle of free movement and wish to restrict EU migration on the other. With regard to the free movement of workers in the context of the UK's withdrawal from the EU, the Netherlands follows the EU's line that free movement is an inseparable part of participation in the single market.

A possible way forward
Even if the relationship between the EU27 and the UK takes the form of a free trade agreement, the free movement of workers will still be an important matter. In exchange for the best possible access to the single market – which the British hope to achieve – the EU27 will want EU workers to be afforded preferential access to the UK labour market. In view of the substantial economic interests at stake for the UK and various EU member states in ensuring free movement as far as possible, the AIV believes that both the UK and the EU27 should aim to afford each other's citizens preferential access over citizens of third countries.

In the negotiations with the UK it is important to keep in mind that the wish to take control of EU migration is primarily political in nature and seems to be about sovereignty as a value in itself. For example, giving evidence to a House of Lords Select Committee, Zsolt Darvas, Senior Fellow at the Bruegel think tank, pointed out that in spite of the

fact that the UK does have control over immigration from third countries, about half of the total number of immigrants since 2004 have come from non-EU countries.[66] In other words, the UK authorities granted these migrants from outside the EU explicit permission to come to the UK, probably because of the expected economic benefit the UK would derive from their work. According to Darvas, therefore, it may be inferred that the objections to EU migration cannot be primarily economic in nature. If the objections are by and large politically motivated, the negotiations will essentially be a matter of setting limits on EU immigration that enable the UK government to argue that it has regained control over its borders.

III.6 Cooperation in the field of education and research

In the area of education and research policy, the possible consequences of Brexit call to mind the consequences of the Swiss referendum on the free movement of persons. The vote by the Swiss to reject free movement meant the end of full Swiss participation in European education and research programmes and caused a great deal of uncertainty for EU students in Switzerland and vice versa and for cooperation in the field of research.[67] The UK's exit similarly has potentially far-reaching consequences for bilateral academic cooperation between Dutch and British knowledge institutions, and for European education and research programmes. In the near future European students will be wondering whether they can complete their studies in the UK at the lower rate of tuition fees applicable to EU students.[68] It was recently announced that the number of applications by EU students to British universities in February 2017 was down by 7% compared with the semester before the referendum on UK membership of the EU.[69] In the longer term the financing of the European research programme Horizon 2020 will come under pressure due to the loss of UK contributions to the EU budget.[70] These developments could all have a very harmful effect on a country like the Netherlands, whose economic growth is highly dependent on the knowledge sector.

UK position

The UK government has tried to reassure the knowledge sector by giving guarantees on, for example, the financing of research projects. The Treasury gave an assurance that 'where UK organisations bid directly to the European Commission on a competitive basis

66 See: <http://bruegel.org/2017/02/brexit-uk-eu-movement-of-people/>.

67 EUPRIO, 'Spotlight: Swiss Immigration Vote Hits Education and Research,' 13 August 2014, consulted on 21 February 2017. See: <http://www.euprio.eu/spotlight-swiss-immigration-vote-hits-education-and-research/>.

68 Carly Minsky, 'How could Brexit impact international students?', *Times Higher Education*, 24 June 2016, consulted on 23 February 2017. See: <https://www.timeshighereducation.com/student/news/how-could-brexit-impact-international-students>.

69 UCAS, 'Applicants for UK higher education down: 5% for UK students and 7% for EU students', 1 February 2017, consulted on 21 February 2017. See: <https://www.ucas.com/corporate/news-and-key-documents/news/applicants-uk-higher-education-down-5-uk-students-and-7-eu-students>.

70 Neth-ER, 'Kennisprogramma's de dupe van Brexit?' [Education and research programmes to be victims of Brexit?], 19 January 2017, consulted on 21 February 2017. See: <https://www.neth-er.eu/nl/nieuws/Kennisprogramma-s-de-dupe-van-Brexit>.

for EU funding projects while we are still a member of the EU, for example universities participating in Horizon 2020, the Treasury will underwrite the payments of such awards, even when specific projects continue beyond the UK's departure from the EU'.[71] As regards the post-Brexit phase, the UK government stated in its White Paper on Brexit that: 'As we exit the EU, we would welcome agreement to continue to collaborate with our European partners on major science, research and technology initiatives.'[72] But the government has not addressed the question of whether it is prepared in this regard to guarantee the mobility of researchers, as a committee of the House of Commons has recommended.[73] The UK position on taking back control of immigration does not increase the likelihood that the mobility of researchers will be guaranteed.

EU position
Although, as already mentioned, the EU institutions have not yet adopted any positions on any issue at all that will be up for negotiation, the Swiss precedent could offer pointers as to the approach that could be adopted towards the UK. In that instance, a representative of the European Commission's Directorate General for Education and Culture (DG EAC) indicated that Switzerland could only take part in European education and research programmes if this provided 'a clear added value for the Union'.[74] This possibility is considered in more detail below.

The Netherlands' position
The Netherlands has a strong interest in continuing bilateral and EU cooperation in the area of education and research. Firstly, the loss of UK contributions will leave a hole in the EU budget that the Netherlands might have to fill (see section IV.1). A continuation of some form of cooperation would – as explained below – open the way for the UK to carry on contributing to the financing of EU education and research programmes. As a result, any increase in Dutch contributions to the EU budget could be limited. Secondly, ongoing uncertainty about the UK's continued participation in European education and research programmes could cause the Netherlands, with its knowledge-based economy, untold collateral damage since the exchange of researchers and students could decrease significantly.

A possible way forward
The AIV sees a short-term and a long-term solution as regards cooperation with the UK in education and research. In the long term, the UK could associate itself wholly or partly with the Horizon 2020 research programme after leaving the EU. In this scenario the UK would need to contribute financially to the programme and conclude a new association agreement for each new framework programme. The UK would then be able to continue

71 HM Government, 'Chancellor Philip Hammond guarantees EU funding beyond date UK leaves the EU', 13 August 2016. See: <https://www.gov.uk/government/news/chancellor-philip-hammond-guarantees-eu-funding-beyond-date-uk-leaves-the-eu>.

72 HM Government, 'The United Kingdom's exit from and new partnership with the European Union', Cm 9417, February 2017, p. 59.

73 House of Commons Science and Technology Committee, 'Leaving the EU: implications and opportunities for science and research', HC 502, 18 November 2016, p. 26.

74 EUPRIO, 'Spotlight'.

to take part in the decision-making processes within Horizon 2020.[75] As regards Erasmus+, the EU's main education programme, the UK can remain involved either as a Programme or a Partner country. As a Programme country, the UK would enjoy full access to the Erasmus+ programmes, while these opportunities would be limited if it opted for Partner country status.

The AIV is of the opinion that continued cooperation in the knowledge field would deliver sufficient added value in view of the academic standing of British educational and research institutions and the fact that the Netherlands and other highly developed EU countries are knowledge-based economies. In the longer term the AIV therefore considers it desirable to reach an agreement under which the UK would be associated with Horizon 2020 and would continue to take part in Erasmus+ as a Programme country.

If it proves impossible to agree on this during the article 50 negotiations, the Swiss precedent offers a way out in the short term. After the Swiss referendum on the free movement of persons, the Swiss government introduced a transitional phase in which it financed the exchange projects that would have received EU funding.[76] A temporary solution was also found for the research projects, buying time to agree on full association with the European education and research programmes.[77] The Treasury's undertaking, mentioned above, to continue financing projects after the UK's departure from the EU that have been promised EU funding, holds out the possibility that, even in the event of a hard Brexit, there will be time thereafter to work towards the long-term solution favoured by the AIV in the field of education and research.

It should be noted that any cooperation agreement on education and research will depend on the UK's willingness to allow the free movement of persons. As in the case of Switzerland, the UK will only be granted full association if it permits free movement.[78] In this regard the AIV remains of the opinion that, as in other policy areas, the EU27's internal cohesion must continue to be the priority. The Netherlands cannot therefore consent to an agreement or partial agreement on cooperation in education and research if this would entail making disproportionate concessions to the UK in other policy areas that other EU member states consider urgent.

III.7 The possible impact of Brexit on the Dutch fisheries sector

It is clear that many economic sectors in the Netherlands will feel the impact of the UK's departure from the EU. And while the fisheries sector may not be the largest among

75 EUA, 'After the "Brexit" Referendum: Possible outcomes for Horizon 2020 and Erasmus+', 9 September 2016. See: <http://www.eua.be/Libraries/publications-homepage-list/after-the-brexit-referendum-possible-outcomes-for-horizon-2020-and-erasmus.pdf?sfvrsn=4>.

76 The Federal Council, 'Interim solution for Erasmus+ in 2014', 16 April 2014. See: <https://www.admin.ch/gov/en/start/dokumentation/medienmitteilungen.msg-id-52695.html>.

77 SwissCore, 'Status of Swiss institutions in EU knowledge programmes', consulted on 21 February 2017. See: <https://www.swisscore.org/swiss-knowledge/ch-status>.

78 Mike Galsworthy and Rob Davidson, 'Debunking the myths about British science after an EU exit', 5 December 2015, consulted on 21 February 2017. See: <http://blogs.lse.ac.uk/brexit/2015/12/05/debunking-the-myths-about-british-science-after-an-eu-exit/>.

them, the adverse consequences it suffers due to Brexit could well be very considerable. This prompted the AIV to give specific consideration to this sector. The AIV has based its consideration in large part on the position paper issued by organisations representing the Dutch fishing industry, namely *Redersvereniging voor de Zeevisserij* (RVZ), *VisNed* and *Nederlandse Vissersbond*.[79]

The position paper outlines three issues that are potentially the most problematic:

a. Access to UK waters

Under the Common Fisheries Policy, which was introduced in 1983, fishermen from EU member states have access to each other's waters, provided they have quotas there. The Dutch fishing fleet's traditional fishing grounds fall largely within the Exclusive Economic Zone (EEZ) extending 200 nautical miles from the British coast. The proportion of the catch caught by Dutch fishermen in UK waters is 70% for the main species of fish. Failure to secure lasting and full access to UK waters in the negotiations with the UK, claims the position paper, will have a major and highly negative impact on the Dutch fisheries sector.

It is therefore of crucial importance to the Dutch fisheries sector that the current access regime can be continued unaltered. Securing unaltered access will require cooperation with other EU member states that have comparable (albeit generally smaller) interests, in particular France, Germany, Ireland, Denmark, Sweden and Belgium.

b. Allocation of fishing quotas among member states

The fishing quotas for relevant, commercial species of fish are shared among EU member states according to distribution keys fixed in 1983. The UK fisheries sector believes that the UK was allocated too low a share of the fishing quotas at the time of the negotiations prior to the UK's accession in 1973 and is urging a re-allocation of the quotas during the Brexit negotiations. If the EU yields to the UK on this point, a re-allocation of quotas in favour of the British will automatically result in a lower share for, and a structural reduction in the size of, the Dutch fisheries sector.

The Dutch fisheries sector takes the view that no argument can be found in the UK's accession in 1973 that would justify altering the allocation of quotas between the UK and EU member states now. The AIV shares this view.

c. Allowing innovative fishing technology: pulse fishing

Dutch fishermen use the technique of pulse trawling, in which brief electric pulses with a very low voltage are employed to induce sole to emerge from the seabed, after which they can easily be caught. In the UK there is an aversion to this kind of pulse technology. As a large proportion of sole is caught by Dutch fishermen in UK waters, a possible ban after Brexit could have a very negative impact on them.

From the perspective of the Dutch fisheries sector, the maximum aim going into the

79 Position paper 'Nederlandse visserijsector bij de Brexit-onderhandelingen' [The Dutch fisheries sector in the Brexit negotiations], RVZ, VisNed, Nederlandse vissersbond. See: <https://www.tweedekamer.nl/kamerstukken/detail?id=2017Z01450&did=2017D03027>.

negotiations should be to ensure that pulse gear can continue to be used without further conditions. For the Dutch fishermen concerned, this is a stark economic necessity.

The Netherlands' position
The Dutch fisheries sector advocates linking the fisheries dossier to other dossiers where the UK has significant wishes (i.e. access to the single market and limiting the free movement of persons). This would maximise the chances of being able to effectively promote the interests of the fisheries sector. The AIV shares this view, but also advocates a balanced weighing up of Brexit's potentially serious impact on the Dutch fisheries sector against the sector's relatively small scale and economic significance to the Dutch economy.

It should also be noted that it is very much in the UK's interest to reach agreement on this specific dossier. While access to UK waters is crucial for many European fishermen, at the same time the UK is highly dependent (68%) on the EU market for the export of fish products. Combined with the UK's wish to have access to the single market, this may offer opportunities for reaching a compromise that limits the potential damage to the Dutch – and European – fisheries sector.

IV Selected topics

IV.1 The EU budget, the multiannual financial framework and Brexit

Political tension
Brexit will not only have a significant impact on the EU budget itself, it may also have far-reaching political consequences for relations within the EU. Former EU Budget Commissioner Kristalina Georgieva referred to the MFF as a seven-year peace treaty.[80] Brexit, when it comes, will unravel the financial agreements on revenue and expenditure that were concluded with so much difficulty. In addition, the negotiations on Brexit's impact on the current MFF will constitute a step towards the negotiations on the next MFF. The matter thus becomes even more politically sensitive.

Although all manner of questions about the impact of Brexit on the EU still remain unanswered, the budgetary and political consequences will in any event be immense. The Irish Prime Minister, Enda Kenny, expects the negotiations to be quite vicious,[81] although hitherto agreement has always been reached in the end, and within a reasonable time frame, on the EU budget. However, the results of some previous budget negotiations have in the long term made inroads into Dutch support for European integration. The Netherlands will be the main requesting party in these negotiations, partly because it is proportionately the biggest net contributor. The departure of one of the other major net contributors – the UK – will probably hit the Netherlands hard. The effect could be aggravated if the rebates disappear in the medium term (in the next MFF).

In the end, the key question on this issue of high politics is how tough the Netherlands is prepared to be in playing the political game.

Three budgets and the relationships between them
Partly on the basis of Mrs May's recent speech about a clean break, the AIV expects to see the UK make a complete exit from the EU in the spring of 2019. The effects on the EU budget can be distinguished on three levels.

1. The divorce bill (or withdrawal bill): settling outstanding accounts

The EU has entered into long-term commitments on the basis of UK membership. A value will have to be assigned to these obligations and outstanding amounts settled. The total divorce bill could amount to €60 billion.[82] This figure represents the UK's share of the total of legal commitments, pension obligations for EU officials and other contractual obligations.

One relevant question is: what will and will not fall within the divorce settlement? If the

80 Schout, A., Y. van Loon (2017), 'European Added Value: Application of Guiding Principles to the EU Budget', Clingendael: Policy Paper.

81 Politico.eu, 4 November 2016.

82 Alex Barker, 'The €60 billion Brexit Bill. How to disentangle Britain from the EU budget', Centre for European Reform, February 2017.

UK leaves midway through 2019, a decision will have to be taken on, for example, what investments, pensions and current policies the UK should contribute to up until the end of the current MFF. This makes 2019 a problem in any case.

Will the bill cover only the pensions of British EU officials or is it reasonable to expect a rich country like the UK, as a former net contributor, to assume ongoing responsibility for the EU's total pension liabilities? In the Brussels corridors of power, they say that the UK cannot dine with everyone else in the restaurant and then walk out before the full bill arrives.[83] However, the UK may opt to focus more narrowly on current commitments.

It is also relevant to consider whether a payment should be made towards the cost of financial plans for 2019 – and 2020 as well. After all, the UK did agree to the MFF, and the MFF is a multi-year budget.

A separate question for the Netherlands is whether the divorce settlement can be used to cover additional expenditures caused by Brexit. Logically speaking, the Netherlands agreed to pay a high net contribution partly on the basis of the UK's contribution. The removal of the UK's contribution will hit the Netherlands hardest of all the member states. The Netherlands could consider including this in the negotiations, together with the other major net contributors. The UK is not just walking out of the restaurant; it is leaving the other major net contributors to pay the bill.

2. The current MFF period (2014-2020)

The UK's commitments for 2019 and 2020 amount to some €15 billion per calendar year (taking account of the rebate). Minus the €4.3 billion that flows back to the UK every year, this means a budget deficit of approximately €10 billion.[84] However, this amount depends on:[85]

- Trade flows and exchange rates. If the UK's trade with continental Europe decreases or if Brexit leads to lower growth in the EU27, this will reduce the EU's income. Normally such a deficit is made up by means of contributions based on gross national income (GNI). This will have an adverse effect on the Netherlands.[86]
- How the member states deal with the potential budget margin. Formally speaking, Brexit means a treaty change, in which case the current MFF should be adjusted 'accordingly'.[87] This raises questions such as: Will all the budget items be adjusted automatically or will allocations be negotiated? Will expenditures and revenues be adjusted equally or will, for example, the EU budget remain the same? The accession

83 *Financial Times*, 12 October 2016.

84 'EU budget and the UK's contribution', House of Commons: Briefing Paper, 1 November 2016.

85 The Norwegian model is disregarded here because it does not provide for a clean break.

86 By way of a detail: since the exchange rate for the pound is low at the moment, the Netherlands now has to contribute more anyway because the UK's GNI is calculated in GBP.

87 Article 20 MFF: 'Adjustment of the financial framework in case of a revision of the Treaties. Should a revision of the Treaties with budgetary implications occur during the financial framework, the necessary adjustments to the financial framework shall be made accordingly.'

of Croatia in 2013 (which is in principle comparable to a withdrawal) meant a compromise in the form of a reallocation of expenditures and a rise in payments (not in commitments: the margin between payments and commitments was reduced).[88]
- If the net recipients succeed in keeping planned expenditure within the current MFF constant, this will have to be compensated for and the deficit to be made up will rise by approximately €15-17 billion.

For the Netherlands this will mean an additional expenditure of between €760 million per year (in the event of a €10 billion loss related to Brexit, but it must be remembered that 2019 will not be a whole year, probably more like 1.5 years) and more than €1 billion per year if the net contributors manage to keep the EU budget at the same level. This represents a sharp increase of 15% to 20% in the Dutch contribution to the EU.

There are various possible scenarios for absorbing the impact of the UK's withdrawal:[89]

- Make cuts in the budget that would fully offset the effects of Brexit. This would require negotiations on how to distribute the cuts across expenditure items. Needless to say, the member states will have widely different viewpoints on this.
- Make up the shortfall in full by means of an increase in GNI-based contributions. Every country would be affected, ranging from an increase of 6% in Ireland's contribution to an extra16.5% for the Netherlands (assuming that Brexit will cost €10 billion).
- New financial instruments. The 'advantage' of this course is that it could perhaps be disguised in the form of an increase in VAT-based contributions.[90]
- A combination of the above. However, it is doubtful whether the Netherlands should agree to every possible combination (see below).

The line taken here will influence the negotiations on the next MFF. In the AIV's opinion, it would be in the interests of the Netherlands to take a tough stance from the outset.

3. The next MFF

The impact of Brexit in the medium term will be more significant than the few remaining years in the current MFF. The net contributors, including the Netherlands, will take the line that the EU budget simply has to be reduced. The net recipients will not be prepared to simply accept this. Compromises and the associated dangers for the Netherlands loom on the horizon.

Another factor here is that the majority of the member states want to abandon the rebate system forced on them by the UK. The Netherlands, Germany, Sweden and Austria are in the minority. Sweden may possibly be appeased by making a distinction between the eurozone budget and the MFF.

The EU institutions, the southern member states and the net recipients will probably

88 'Brexit and the EU budget', *Notre Europe*, 16 January 2017, p. 12. European Commission, EU public finance, 5th edition, Luxembourg: Publications Office of the European Union, 2014, pp. 93-94.

89 See for example: *Notre Europe*, ibid.

90 For other new financial instruments or EU taxes, see the Monti report of January 2017.

aim for deeper integration in the case of the EU budget as well as elsewhere, in the form of own resources that resemble EU taxes. A compromise on new types of revenue (EU taxes) is certainly very possible. The negotiations involved will undoubtedly be very painful for the Netherlands.

In the AIV's opinion, the UK's withdrawal should result in a reduction in EU expenditure in proportion to the size of the UK's net contribution to the EU budget, since without the UK the volume of the EU's economic output will fall in absolute terms, which should be reflected in the level of the EU budget. The Netherlands should join the other net contributors in making a case for this view in the negotiations. The Netherlands and the rest of the EU27 should prepare for tough budget negotiations. In this connection it is also essential for the Netherlands to be heedful of the level of domestic support for the EU in the long term.

IV.2 The position of the Court of Justice

UK and EU position
On 17 January 2017, as mentioned above, Prime Minister Theresa May stated explicitly that after leaving the EU the UK will no longer recognise the jurisdiction of the Court of Justice of the EU and that the UK's laws would be made and interpreted in Britain. Full Brexit will probably not take place until after a transitional period. The House of Commons cross-party select committee on Brexit also took the view that Mrs May should reach agreement with the EU on a transitional arrangement in order to avoid a cliff edge.[91] The role of the CJEU during this transition period is now emerging as a politically fraught issue in the debate.

For the EU, chief negotiator Michel Barnier has for the time being expressed himself in guarded terms, by saying that an overly comfortable transition is to be avoided. Nor has the European Council as yet adopted an official position on this matter. However, after Malta took over the EU presidency on 1 January 2017, the Maltese Prime Minister Joseph Muscat became the first EU leader to express his views, when he stated on 12 January that the application of EU law and the jurisdiction of the CJEU must be essential parts of any transitional deal with the UK: 'It is not a transition period where British institutions take over, but it is a transition period where the European Court of Justice is still in charge of dishing out judgments and points of view.'[92] He added: 'It would be quite stupid to settle for EU membership if it is then inferior to the Brexit arrangements. That is something that is keeping us together.'

European diplomats posted to the UK who use the Foreign and Commonwealth Office (FCO) as a sounding board have also cautioned that the UK cannot withdraw from CJEU jurisdiction during the transition period.[93] Staff of the European Commission's Legal Service have declared that EU law must be available to EU citizens after Brexit, under

91 See: <https://www.theguardian.com/politics/2017/jan/14/brexit-committee-demands-transitional-deal-and-parliamentary-vote>.

92 See: <https://www.theguardian.com/politics/2017/jan/12/eu-law-will-continue-to-apply-in-uk-during-transition-deal>.

93 See: <https://www.theguardian.com/politics/2017/feb/03/brexit-transition-uk-eu-law>.

the jurisdiction of the CJEU.[94] On 1 February 2017, the President of the Court of Justice, too, clearly stated that it is highly likely that at some point national courts will bring aspects of the future trade agreement with the UK before the CJEU. What aspects might arise is unknown and will depend on what questions parties refer to the Court for a preliminary ruling under article 267 TFEU. As noted in the *Independent*: 'His comments, however speculative, expose the very real possibility that Britain's exit from the EU could be shaped under the jurisdiction it is determined to escape.'[95] This is diametrically opposed to the view of some Eurosceptics, including ministers in the UK government, that the UK Supreme Court could have the last word on the interpretation of any transitional arrangement.

Against this background it is noteworthy that neither Mrs May's Lancaster House speech nor the Brexit White Paper of 2 February 2017 discusses the role of the CJEU in a transitional period of this kind. The options for dispute settlement outlined in the White Paper concern the free trade agreement to be concluded between the UK and the EU, and do not specifically refer to a transitional arrangement. Mrs May will find it difficult to accept the jurisdiction of the Court in any transition, since that would make it impossible for her to keep her promise that the UK will have regained full sovereignty by 2019, one of her key political objectives with a view to the general election in 2020. There have however been reports of statements by senior staff of the Department for Exiting the European Union (DExEU) that 'a special joint court' may be necessary to settle disputes during the transition period.[96]

Possible ways forward
The positions of the UK and the EU in this area are quite far apart. The question is therefore whether a compromise is possible. The White Paper does give pointers for the discussion, albeit not specifically concerning a transitional arrangement, by referring to a number of mechanisms provided for in other trade agreements. From these it is possible to distil certain elements that may inform the UK government's position in negotiations on a future dispute resolution mechanism:

- first, attempt through governmental discussion, cooperation and consultation to arrive at a common interpretation of an agreement, for example in the framework of a joint committee;
- establish some form of arbitration panel;
- exclude direct effect, i.e. a mechanism that provides for dispute resolution solely between the states parties, meaning that citizens cannot bring provisions in the forthcoming agreement before either the dispute resolution body or the UK courts;
- rule out a one size fits all solution, in view of the statement that 'different dispute resolution mechanisms could apply to different agreements, depending on how the new relationship with the EU is structured. Any arrangements must be ones that

94 See: <http://www.telegraph.co.uk/news/2016/12/12/exclusive-european-citizens-living-uk-should-remain-jurisdiction/>.

95 See: <http://www.independent.co.uk/news/world/europe/uk-post-brexit-trade-deal-eu-european-court-of-justice-president-a7557116.html>.

96 See: the *Independent*, 3 February 2017.

respect UK sovereignty, protect the role of our courts and maximise legal certainty, including for businesses, consumers, workers and other citizens.'[97]

Although the White Paper refers to a number of trade agreements and their dispute resolution mechanisms – in particular CETA, NAFTA (North American Free Trade Agreement), Mercosur and the WTO – it also makes clear that these should serve merely as examples and not as precedents in the forthcoming negotiations. The UK is aiming for a tailor-made solution which does not necessarily involve a single dispute resolution mechanism.

From the perspective of the remaining member states and the EU, other elements can be identified which play or should play a leading role in seeking solutions in this area and in devising the eventual mechanism for resolving disputes and enforcing agreements. In the AIV's view, these are based on the following considerations:

- the solution chosen should not serve as a negative precedent for other member states (in other words, the solution should not bring the UK benefits at no cost);
- the solution should not needlessly complicate the existing system;
- the solution chosen should afford the best possible protection for the rights of EU citizens and enterprises (not only legal certainty) in accordance with article 20 ff. TFEU on the rights of citizens of the Union;
- there should be guarantees that shared problems and interests can still be addressed as effectively as possible.

To illustrate the last point, it is relevant that while the White Paper stresses that the UK 'will continue to work with the EU to preserve UK and European security, and to fight terrorism and uphold justice across Europe', a recent report ('Brexit: future UK-EU security and police cooperation') by the House of Lords European Union Committee observed: 'Even with the utmost good will on both sides, it seems inevitable that there will be practical limits to how closely the UK and the EU27 can work together on police and security matters if they are no longer accountable to, and subject to oversight and adjudication by, the same supranational institutions, notably the Court of Justice of the European Union.'[98]

This raises the question of whether – at least in certain areas – the UK and the EU will nevertheless have to agree on limited jurisdiction for the Court to make it possible to continue to tackle problems such as Europe's internal security effectively. This could accord with the UK's approach involving different dispute resolution mechanisms for different agreements while not ruling out the possibility of direct effect.

A more general approach that could do justice to all positions in accordance with the principles mentioned above would be to assign the interpretation and application of a future transitional arrangement to a special chamber of the CJEU, which would be the sole body competent to hear such disputes in line with rules and procedures to be agreed – even though politically speaking this would be a hard sell for Mrs May.

97 See: <https://www.gov.uk/government/publications/the-united-kingdoms-exit-from-and-new-partnership-with-the-european-union-white-paper>.

98 See: <https://www.publications.parliament.uk/pa/ld201617/ldselect/ldeucom/77/77.pdf>.

AIV proposal for the Netherlands' position
The AIV believes that a distinction should be made between the interpretation of the article 50 decision on the one hand and on the other the oversight of the UK's implementation of the arrangements and obligations undertaken for the transitional period. Lastly, a distinction should also be made in respect of the future free trade agreement between the UK and the EU.

As regards the interpretation of the article 50 decision, the jurisdiction of the CJEU should remain intact, since this will be a decision by the EU institutions taken on the basis of the Treaty. It is entirely possible that national courts will seek a preliminary ruling on the scope of a particular provision of this decision.

When it comes to oversight of implementation by the UK, everything depends primarily on the depth and breadth of the transitional arrangement and the agreements reached on this point. Ultimately, once the article 50 decision has entered into force, the UK will be a third country. The transitional regime proposed by the AIV in this report can best be compared to the EU's arrangement with Switzerland, with the proviso that the AIV's proposal is based on a temporary continuation of the customs union and the common external tariff. If, as in the case of Switzerland, agreement is reached on mutual recognition of norms and standards, appropriate oversight and a dispute resolution system will be advisable. As yet, the EU's arrangement with Switzerland provides for neither efficient oversight nor a dispute resolution mechanism. However, the Commission hopes to introduce an integrated dispute resolution mechanism based on the WTO's Dispute Settlement System.

V The effects of Brexit on coalition forming in Europe

Current situation
In many areas, the UK is an important partner for the Netherlands in the EU as it is today. Examples include the single market, where the two countries share a desire for completion of the single market and better legislation, and trade policy, where both countries strongly oppose protectionism. In addition, both countries are major net contributors and have largely similar views on, for example, development cooperation.[99]

An evaluation by the Policy and Operations Evaluation Department (IOB) in 2014, entitled 'Towards a strategic approach: Dutch Coalition-Building and the "Multi-Bi Approach" to Influencing EU Decision-Making (2008-2012)' reveals the policy fields in which the Netherlands acted together with other EU member states. It did so most frequently with the UK, Sweden and Denmark.[100] During this period the Netherlands clearly belonged to a North-West Europe group, along with the UK, Sweden, Denmark, Finland, Austria and Luxembourg. The most remote group comprised France, Italy, Spain, Portugal and Greece.[101]

Forming coalitions in the context of the Brexit negotiations
The IOB evaluation mentioned above shows that a coalition is effective only if at least one of the three big member states – Germany, France or the UK – is on board.[102] This has consequences for various policy areas in which the Netherlands has hitherto worked closely and formed part of a coalition with the UK.

A bloc of North-West European countries could be formed to achieve a transitional period for trade in goods, which is of vital interest to the Netherlands. Germany's position and leadership would be crucial here, and the Netherlands could support and strengthen that leadership as a partner of Germany. A bloc encompassing Denmark, Belgium (particularly Flanders), Ireland and the Netherlands would not be powerful enough to exact compensation for the potentially considerable loss of the trade in goods with the UK.

In the field of the free movement of workers, the interests of the Netherlands on the one hand and a number of Central and East European countries on the other are sharply divergent. These interests will have to be balanced if no agreement can be reached with these countries on possible restrictions on the free movement of workers. One possibility could be to persuade the countries in question to agree under pressure from a potential reduction in the cohesion and structural funds in the new MFF or on the basis of pledges to continue defence cooperation (in accordance with the UK's threat expressed in the Lancaster House speech). In this connection moderation will be key,

99 IOB Evaluation, Strategie bij benadering. Nederlandse coalitievorming en de multi-bi benadering in het kader van de EU-besluitvorming (2008-2012) ['Towards a strategic approach: Dutch Coalition-Building and the "Multi-Bi Approach" to Influencing EU Decision-Making (2008-2012)'], July 2014, p. 119.

100 Ibid., p. 111.

101 Ibid., p. 112.

102 Ibid., p. 83.

to ensure that the Central and East European countries maintain their support for the 'same pay for the same work in the same place' agenda, which is important to the Netherlands. It is in the interests of both the Netherlands and many Central and East European countries to safeguard the rights of their nationals who are resident in the UK. A point to consider here would be whether to follow up on the process of reviving cooperation between the 'Inner Six', the original member states, reflected for example in their meeting immediately after the UK referendum.[103]

One other fundamental choice may create differences of opinion between countries or groups of countries during the Brexit negotiations. On the one hand, there is the principle of 'nothing is agreed until everything is agreed', with the accompanying uncertainty about the possibility of a last-minute veto, particularly from those who want to use Brexit for deterrent effect. On the other, there is the desire to keep the option of interim agreements open, which involves the risk that the UK will try to drive a wedge between individual or groups of member states. The AIV considers it vital for the EU27 to maintain a united front during the negotiations and therefore advocates aiming to achieve a comprehensive agreement.

Forming coalitions in the EU27 after Brexit
Once the UK has left the EU it will be even more important for the Netherlands to form part of various coalitions, depending on the policy field and/or the subject at issue. In the AIV's view, this should involve a strategic assessment. The Netherlands could choose, for example, to join a coalition to form a blocking minority in a particular policy area or to find allies for new initiatives.

As regards the EU's future policy on trade with third countries, the UK's departure will probably mean an increase in the influence wielded by the group of more protectionist member states. To counterbalance this trend, the Netherlands should form a coalition with the UK's main trading partners, especially Ireland and the Benelux. This coalition could form a blocking minority by persuading Germany to continue supporting a free trade policy for the EU.

In the area of the CFSP and CSDP, the AIV sees opportunities for deep cooperation with Belgium (particularly in terms of the navy and the air force) and with Germany (particularly in terms of the army). With these countries, the Netherlands could seek other like-minded countries that support stronger CFSP cooperation. On the other hand, it would be possible to refrain from a general move towards closer cooperation within the EU in this area in favour of forming a core group within European defence cooperation. Minister of Foreign Affairs Bert Koenders called for a core group of this kind in the speech he gave at the presentation of the Strategic Monitor 2017 published by the Netherlands Institute of International Relations Clingendael.[104] After Brexit, core

103 See: <https://www.nrc.nl/nieuws/2016/06/25/oprichters-eu-onderhandelingen-brexit-snel-beginnen-a1406284>.

104 Government of the Netherlands, 'Toespraak minister Koenders bij presentatie Strategische Monitor Clingendael/HCSS' (Speech by foreign minister Bert Koenders at the presentation of the Strategic Monitor published by the Netherlands Institute of International Relations Clingendael and the Hague Centre for Strategic Studies), 20 February 2017, p. 11. See: <https://www.rijksoverheid.nl/binaries/rijksoverheid/documenten/toespraken/2017/02/20/toespraak-minister-koenders-bij-presentatie-strategische-monitor-clingendael-hcss/Speech+M+bij+presentatie+Strategische+Monitor.pdf>.

groups in certain policy fields could thus constitute an alternative strategy to building coalitions within the EU.

The role of Germany in any new coalition is crucial in practically all policy areas, partly in view of the importance of the Franco-German axis, on which the UK has regularly exercised a calming influence. Although the importance of the axis has declined in recent years, it may soon increase significantly again depending on the outcome of this year's elections in France and Germany. The AIV therefore regards it as essential for the Netherlands to continue to invest in good relations with Germany and, albeit to a lesser extent, with France. The AIV's view on this point is in line with the IOB evaluation referred to earlier, which identified Germany and the UK as being more of like mind with the Netherlands than France, while France often acted as the leader of an opposing coalition. Nonetheless, the evaluation pointed out that the picture is not quite so clear cut. The AIV agrees with the IOB that the Netherlands is definitely of like mind with France on important subjects such as enlargement, Justice and Home Affairs and parts of the EU's multiannual budget, and that this like-mindedness is sometimes underestimated. However, this does not alter the fact that France is more remote from the Netherlands than Germany and the UK in terms of language and political and administrative culture.[105]

Nor can France be disregarded when the Netherlands is seeking to form a coalition to back the introduction of a new EU initiative. Here the AIV also sees opportunities for renewed Benelux cooperation. The Benelux has a certain status in the Council which partly derives from historical precedents relating to new, small-scale initiatives in cross-border cooperation. While seeking a coalition with France, the Netherlands could therefore also investigate whether Benelux cooperation, which has been less close in recent years, offers scope for building additional coalitions within the Council or – via Luxembourg and Belgium which tend to be oriented towards France – could help to build a bridge between the Netherlands and France.

Another option would be for the Benelux countries to look to the countries of North-West Europe, especially Ireland, Denmark, Finland, Sweden and possibly the Baltic states, with a view to forming a substantial bloc within the EU on various dossiers. In the AIV's opinion, whether this is feasible and desirable should be explored further in the near future.

It should be noted that not only Brexit but also the recent election of Donald Trump as President of the United States will be a factor in the question of possible coalitions. President Trump's election and policies may prompt the Netherlands to retreat to a certain extent from its traditional transatlantic outlook and to orient itself more towards Germany in economic, geopolitical and security terms. In addition, the departure of the UK will see an increase in the importance of other larger member states besides Germany and France, including Spain. The AIV can see scope for stepping up Dutch cooperation with Spain as well, particularly in the economic field.

It is clear from the foregoing that in future coalitions will be less well defined and will depend very largely on the policy field and the subject concerned. That is why the AIV believes it vital for the Netherlands to strengthen its missions in the member states' capitals with a view to potentially building coalitions – ad hoc, task-specific or geographical – in relation to day-to-day decision-making. If the Netherlands is to continue

105 IOB Evaluation, p. 193.

to be a significant player in the EU27, the AIV believes that Dutch embassies in the member states must have sufficient capacity to represent Dutch interests effectively and to be able to forge and/or strengthen coalitions, where necessary and possible. That the Netherlands is well able to do so is clear from the case studies conducted by the IOB, which show the country to be active in forming ad hoc coalitions, mobilising like-minded member states and promoting joint action.[106]

106 Ibid., p. 117.

VI Conclusions and recommendations

VI.1 Conclusions

The questions that the government put to the AIV on 6 October 2016 concerned the key elements of both the new relationship between the EU and the UK and the new bilateral relationship between the Netherlands and the UK. The AIV believes that the key elements of the new bilateral relationship will depend to a significant extent on what form the new EU-UK relationship takes. Accordingly, the latter relationship forms the starting point for this advisory report and is discussed in more depth and detail.

In the new relationship between the EU and the UK, future trade relations will be crucial to both parties. The AIV is of the opinion that the Comprehensive Economic and Trade Agreement between the EU and Canada (CETA) offers the best point of departure in this respect. The AIV believes it would be politically feasible to raise future cooperation in accordance with this model to a higher level by adding elements of the association agreements that the EU has concluded with neighbouring countries. A CETA-plus model along these lines would not only make free trade in goods possible, but would also open the way to agreements on the liberalisation of service sectors. In order to permit an orderly transition to the period following a definitive agreement, the most obvious course of action, in the AIV's view, would be to continue the existing customs union for, say, three years. As regards dispute settlement, an option would be an arbitration system based on the WTO Dispute Settlement System or similar systems in existing free trade agreements.

With regard to financial services, the AIV believes that the prime concern is to minimise disruption to the financial system within the EU and to mitigate as far as possible the negative effects of Brexit on the financial services system. Decisions on third-country regime (TCR) equivalence could be a fall-back position here, although such decisions are not applicable to all financial services and may be withdrawn by the Commission. The advantage is that this approach can in principle be applied to all third countries and hence does not infringe the most favoured nation principle. The scope of equivalence could also be extended, thus rendering this option still more attractive.

In terms of external security, the EU should continue to involve the UK wherever possible in the preparation and implementation of the CFSP and the CSDP. This would undoubtedly be in the interests not only of the UK but also of the EU. Given the intergovernmental nature of cooperation in this field, the AIV believes that exploring avenues for future cooperation should be easier than shaping future trade relations, where the EU institutions will also be involved. The nature of future cooperation on external security will of course partly depend on whether the UK aims to remain involved in the CFSP/CSDP. The advisory report outlines four possible models in this regard. In the AIV's view, it is essential to keep the UK involved in some way in the decisions of the EU Foreign Affairs Council.

In the field of internal security (Justice and Home Affairs cooperation), continued cooperation would likewise be in the interests of the UK, the EU and the Netherlands. Indeed, it is the UK's express aim to continue this relationship. However, it is not yet clear what form cooperation in this field could take in the future. In this connection, it will be crucial to reach agreement on a form of judicial review, but the British intention

to end the jurisdiction of the Court of Justice of the EU (CJEU) in the UK after Brexit is expected to present a serious obstacle to agreement on this point.

Even if the relationship between the EU27 and the UK takes the form of a free trade agreement, the free movement of workers will still be an important matter. In exchange for the best possible access to the single market – which the British hope to achieve – the EU27 will want EU workers to be afforded preferential access to the UK labour market. In view of the substantial economic interests at stake for the UK and various EU member states in ensuring free movement as far as possible, the AIV believes that both the UK and the EU27 should aim to afford each other's citizens preferential access over citizens of third countries.

As regards Brexit's budgetary impact on the EU and specifically on the Netherlands, it is useful to distinguish between the 'divorce bill', the current multiannual financial framework (MFF) period (2014-2020) and the following MFF. Clearly, the Netherlands faces the possibility of a substantial negative financial impact at all three levels. The obvious course is therefore for the Netherlands to adopt a firm stance from the beginning of the negotiations, preferably with other countries (such as Germany, Sweden and Austria) which, as net contributors, are liable to face the most serious negative impact.

When it comes to the CJEU, the hard line taken by the UK, namely that it will not accept the Court's jurisdiction after Brexit, will create serious problems. The Court's position in the probable transitional period is of special concern here. It is uncertain whether the British idea of a special joint court will also be acceptable to the EU. The exact form of the tailor-made solution advocated by the UK is not yet clear. It might be difficult for Prime Minister Theresa May to sell the option of a special chamber of the CJEU which would be the sole body competent to rule on the interpretation and application of the transitional arrangements in accordance with rules and procedures agreed for this purpose.

What is clear is that the Netherlands will lose an important partner when the UK leaves the EU. Aiming to strengthen existing coalitions, such as the Benelux and the partnership in North-West Europe, is desirable but not sufficient. The position of Germany, which should as far as possible form part of the bloc to which the Netherlands belongs, is particularly crucial here. The AIV is aware that Germany has many interests and potential partners, both to the east and in the Franco-German axis. Close cooperation with Germany will thus not always be possible. This is one reason why the AIV argues that the Netherlands should also actively seek partners for ad hoc coalitions on specific dossiers in big EU countries such as France and Spain, but also in smaller countries such as the Baltic states, preferably as part of a bloc of North-West European countries.

VI.2 Recommendations

1. The AIV believes that the process of shaping the new relationship between the EU and the UK should centre on the long-term importance of continuing close European cooperation against the background of the economic and geopolitical shifts that are currently under way and the enormous external challenges now facing the EU countries. Cooperation between the EU27 and the UK will remain vital in order to guarantee security, freedom and welfare in Europe, and to help to provide stability and prospects for people in Europe's neighbouring countries.

2. The AIV considers it vital for the EU27 to maintain a united front during the article 50 negotiations. This means that the Netherlands should not appear receptive to any British proposals evidently intended to play EU member states off against one another.

3. As regards the withdrawal agreement, the AIV thinks it is essential for the government of the Netherlands to concentrate its efforts on the position of EU citizens in the UK and UK citizens in the EU, and on the size of the exit bill.

4. On the subject of future relations, the AIV is of the opinion that the EU should aim for a comprehensive free trade agreement with the UK, similar to the agreement with Canada (CETA), if possible supplemented by elements of more far-reaching economic integration like those enshrined in the association agreement with Ukraine.

5. Since it is unlikely that agreement can be reached on a comprehensive free trade agreement within two years, notwithstanding the position taken by the UK, the AIV believes that a short transition period would be both probable and desirable, to allow an orderly transition between the UK's actual exit from the EU and the conclusion of a free trade agreement of this kind. The AIV therefore argues that the customs union should remain in place for three years, if possible with continued mutual recognition of norms and standards.

6. As regards financial services, the AIV believes that an equivalence system would be the most probable and realistic solution to the loss of passporting rights. The Netherlands should also strive for solid arrangements during the transition period, to minimise the damage to business.

7. The UK's withdrawal also represents a significant loss to the EU's external security, especially for the Common Foreign and Security Policy (CFSP) and the Common Security and Defence Policy (CSDP). The AIV therefore believes it essential for the government to push for EU-UK cooperation to continue, albeit in another way, and to work actively towards this goal, for example by involving the UK in some way in the decisions of the EU's Foreign Affairs Council.

8. Given the great importance that should be attached to keeping the UK closely involved in certain forms of European military cooperation, whether multilateral or bilateral, the AIV would argue that the government should continue the existing bilateral ties with the UK. Military cooperation with the UK should be assessed on its own merits and should not suffer from possible friction between the EU and the UK concerning trade policy.

9. When it comes to internal security, in other words Justice and Home Affairs cooperation, the AIV also believes that continuing the existing cooperation is essential to the internal security of both the UK and the EU, particularly the Netherlands. However, the position of the CJEU is a complicating factor here, for which a practical solution has yet to present itself.

10. In the AIV's view, the EU member states would do well not to link initiatives aimed at improving the functioning and the fairness of the free movement of workers within the EU to the Brexit negotiations. Arguments by the Netherlands and other mainly Western European member states in the context of the revision of the Posting of

Workers Directive, to ensure the same pay for the same work in the same place, would then possibly still stand a chance of being accepted by the member states in Central and Eastern Europe. This cause is unlikely to be helped by combining it with the divergent British wish to limit the number of migrants from the EU.

11. If the UK is to participate in the single market for goods during a transitional period, it will be necessary to ensure the continued adoption and equivalent practical application of the single market acquis. If the UK does not recognise the jurisdiction of the CJEU during this period, the AIV believes it will be necessary to set up an appropriate system for oversight and dispute settlement.

12. Brexit may have a major impact on the Netherlands in financial terms, too. During the forthcoming negotiations on the new MFF, the AIV takes the view that the Netherlands, together with other net contributors, should seek ways of reducing the EU budget over the coming years, so as to ensure that the Dutch contribution remains the same and in any event does not increase.

13. The UK has been a natural coalition partner for the Netherlands on several dossiers (the single market, trade and defence cooperation, for example). After Brexit, the Netherlands will have to focus more closely than before on other possible coalition partners. The AIV thinks the Netherlands should aim for close cooperation and coordination with Germany, the most influential member state in the EU, but that will not be enough. Other possible coalition partners include the countries of North-West Europe, particularly Sweden, Denmark and Ireland, but also (in the framework of enhanced Benelux cooperation) Belgium and Luxembourg. Ad hoc coalitions would also be advisable, for example with bigger EU countries like France and Spain, but also with the Central and Eastern European countries, for instance in the field of security.

Request for advice

Mr Jaap de Hoop Scheffer
Chairman of the Advisory Council
on International Affairs
P.O. Box 20061
2500 EB The Hague

Date 6 October 2016
Re Request for advice on Brexit

Dear Professor de Hoop Scheffer,

On 23 June a referendum was held in the United Kingdom on the country's EU membership in which 51.9% of British voters voted to leave the EU and 48.1% voted to remain. The government respects this outcome, though it is disappointed that a majority of those voting preferred to leave the EU. Since 1973 the UK has been a valued member of the EU and an important European partner for the Netherlands. The Netherlands and the UK have a close relationship and work together in a variety of areas: political, military, economic, cultural and social. With this in mind the government has consistently sought to keep the United Kingdom within the EU fold.

It is now up to the British government to indicate how it intends to deal with the referendum result. The UK can only withdraw from the EU once it has followed the applicable procedure set out in article 50 of the Treaty on European Union. This process will start as soon as the UK formally states its intention to invoke the article (the 'notification procedure'). Pursuant to article 50 there will then be negotiations on a withdrawal agreement. As soon as the withdrawal agreement takes effect, the EU treaties will no longer apply to the UK. If no such agreement has been reached within two years of notification, the EU treaties will automatically cease to apply to the UK, unless this time span is extended by the EU and the UK. At this point it would be prudent to consider what the shape of our future relationship with the UK should be.

In the light of the above, the government would ask the Advisory Council on International Affairs (AIV) to provide an advisory report by next spring at the latest that addresses the following questions:

1. From the Netherlands' perspective, what should be the key elements of the new bilateral relationship with the United Kingdom?
2. From a Community perspective, what key elements should be part of the EU's new relationship with the United Kingdom?
3. What implications do the elements referred to in the previous two questions have for Dutch interests and the formation of coalitions within Europe?
4. What should the Dutch government's aims be in its bilateral relationship with the UK in the next several years?

I look forward to receiving your report.

Yours sincerely,

Bert Koenders
Minister of Foreign Affairs

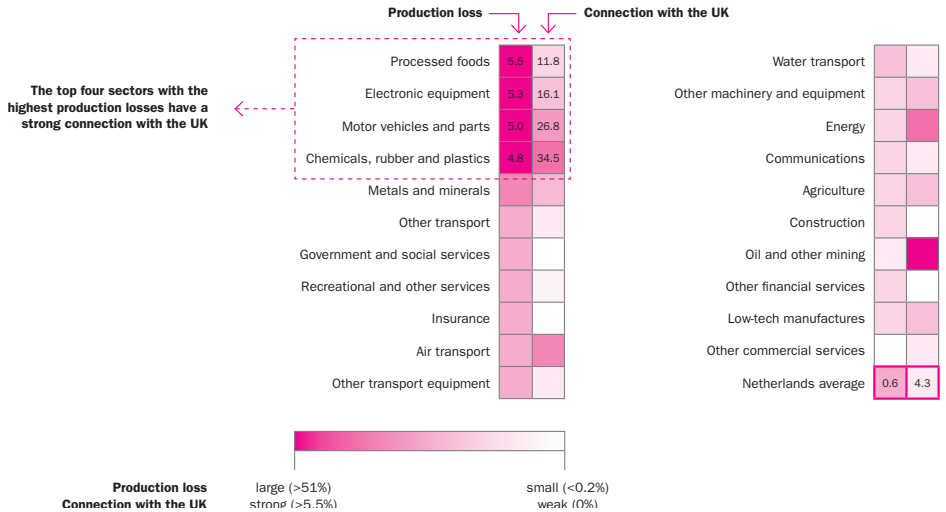
The cost of Brexit to the Netherlands

General estimates

According to the CPB, the cost to the Netherlands of Brexit is 'relatively high' compared with other EU member states.[107] In the WTO scenario, its estimate of the cost indicates a GDP loss of 1.2% in 2030. This is equivalent to €10 billion or €575 per head of the population. If the loss of trade with the UK is coupled with an innovation loss, the cost rises in the WTO scenario to a GDP loss of 2%, or €1,000 for every Dutch resident.[108] In the FTA scenario, the cost to the Netherlands is lower, with a GDP loss of between 0.9% and 1.5%.[109]

Sector-specific and other consequences

In the WTO scenario, there are big differences between sectors in the impact of Brexit: the loss of production will be some 5% in the sectors whose connection (as defined below) with the UK is more than 10%, i.e. chemicals, rubber and plastics; electronic equipment; motor vehicles and parts; and processed foods. These sectors together earn 12% of GDP. The costs are shown in the diagram below.[110]



NB: connection with the UK = (sectoral imports from and exports to the UK) / (sectoral GDP multiplied by 2).

Indirect exports, consisting of goods in transit via the Netherlands and exports of Dutch semi-finished products, may also be adversely affected by new impediments to trade. The mineral extraction, wholesale, retail and business services sectors in particular have a greater share of production that is ultimately consumed by the UK than is exported direct to the UK.[111] However, the costs of a possible loss have not yet been established.

107 J.C. Bollen et al., 'Brexit raakt Nederland meer dan meeste EU-landen' [The Netherlands will be harder hit by Brexit than most EU countries], CPB Policy Brief 2016/07, pp. 8-9.

108 Ibid., p. 9.

109 Ibid.

110 Ibid., p. 12.

111 Carlijn Prins and Lisette van de Hei, 'Wat betekent een Brexit voor het Nederlandse bedrijfsleven?' [What will Brexit mean for Dutch business?], Rabo Research, 15 June 2016, pp. 7-8.

List of persons consulted

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Albert van der Horst	macroeconomic analysis sector head at the Netherlands Bureau for Economic Policy Analysis (CPB)
Lord Jay of Ewelme	member of the House of Lords, member of the Lords European Union Committee
Dorothée van Kempen	policy officer for EU affairs at the Ministry of Security and Justice
Ronald Kent	managing director, wholesale & financial policy, and head of Brexit policy at the British Banking Association (BBA)
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Jochem Wiers	head of the Brexit task force at the Ministry of Foreign Affairs
Alexander Wright	deputy head of the Foreign and Security Policy Unit, Europe Directorate, FCO
Diederik Zandstra	senior policy director, Brexit, BBA

List of abbreviations

AFSJ	area of freedom, security and justice
AIV	Advisory Council on International Affairs
BRRD	Bank Recovery and Resolution Directive
CEAS	Common European Asylum System
CETA	Comprehensive Economic and Trade Agreement
CFSP	Common Foreign and Security Policy
CFTA	comprehensive free trade agreement
CJEU	Court of Justice of the European Union
CPB	Netherlands Bureau for Economic Policy Analysis
CSDP	Common Security and Defence Policy
DExEU	Department for Exiting the European Union
EAW	European Arrest Warrant
ECRIS	European Criminal Records Information System
EDA	European Defence Agency
EDF	European Development Fund
EEA	European Economic Area
EEAS	European External Action Service
EFTA	European Free Trade Association
EMA	European Medicines Agency
EMU	Economic and Monetary Union
EP	European Parliament
EU	European Union
EU27	EU member states excluding the United Kingdom
FCO	Foreign and Commonwealth Office
FTA	free trade agreement
GATS	General Agreement on Trade in Services
GATT	General Agreement on Tariffs and Trade
GDP	gross domestic product
GNI	gross national income
GNP	gross national product
IMF	International Monetary Fund
IOB	Policy and Operations Evaluation Department
JHA	Justice and Home Affairs
MFF	multiannual financial framework
MFN	most favoured nation

NATO North Atlantic Treaty Organisation

SIS Schengen Information System

TEU Treaty on European Union

TFEU Treaty on the Functioning of the European Union

UK United Kingdom

UN United Nations

US United States

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