

The Malthouse Compromise

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The recent vote in parliament attempting to prevent a no-deal outcome on Brexit was counter-productive and non-binding. Any attempt to hobble the government's negotiating hand would have been a self-inflicted wound. It was also irrelevant, since virtually no-one in the UK is advocating no deal. The preference of the European Research Group (ERG) of Conservative Eurosceptic MPs has always been for what is usually called a 'Canada-plus' free trade agreement. Everyone also supports sensible side deals on such issues as aircraft landing rights, air and vehicle safety certification, and trucker's licences. It may not be the Withdrawal Agreement signed off by Theresa May, but it is a perfectly coherent UK offer, especially if accompanied by undertakings on the Irish border.

It is entirely logical for Brussels to play hardball at this stage of the talks. The EU still sees some prospect of Parliament reversing its rejection of the Withdrawal Agreement and is, of course, fully aware of the non-binding vote on no deal. However, the EU's current refusal to re-open the Withdrawal Agreement is unlikely to be a guide to the endgame in March.

It would nevertheless be logical for the EU to offer Parliament a sweetener in the form of a codicil attached to the Withdrawal Agreement. This codicil could suggest that the EU will try hard to ensure that the backstop is either never used or will be used for only a short period (where the EU has done similar things in the past). However, this is unlikely to work since prominent ERG MPs have said that they will reject any formulation that does not replace the current wording of the Withdrawal Agreement with a clear get-out clause from the backstop. The likelihood is thus that the deal will once again be rejected if it returns to parliament.

The prime minister's first preference is clearly still to get an amended Withdrawal Agreement through parliament. Her strategy all along has been to give Leave supporters a formal exit from the EU and control

over EU migration, but to give companies an outcome very close to the customs union and single market. The recent Nissan decision not to build the new X-Trail model in the UK will have strengthened this resolve.

The voting strength of the ERG, however, means that a fall-back position is now under consideration – the ‘Malthouse Compromise’. This is close to the ERG’s longstanding preferred option, with the involvement of prominent Remainers giving the plan a far higher profile than we might otherwise have expected. These MPs find the Withdrawal Agreement unacceptable. They also share a survival instinct and wish to prevent their party from fracturing and losing the next election. If and when the Withdrawal Agreement fails again to pass in Parliament, the plan is to have a compromise which the Malthouse group hope will command sufficient Tory and DUP support (together with up to forty Labour MPs from leave-voting constituencies) to provide majority backing in parliament. This can then be presented to the EU who will need to choose between this and no deal.

The Malthouse Compromise is based on a free-trade agreement with no tariffs or quotas. A commitment to avoid new infrastructure on the Irish border is supported by proposals for advanced customs and trade facilitation measures of the sort already in use on, for instance, the Swiss border. Regulatory equivalence of the type that currently exists for meat imports from New Zealand are proposed to remove the need for sanitary and phytosanitary checks for food and animal imports. Non-regression clauses of the sort common in modern free trade agreements are proposed to address EU concerns over unfair competition. Provisions on citizen’s rights and payments to the EU would be carried forward from the Withdrawal Agreement.

The Malthouse plan could involve an extended transition period agreed under article 50 to allow time to negotiate a free-trade agreement (which should not be difficult between two entities which already have free trade). Additional payments would accompany an extended period. Alternatively, the free trade negotiation could be conducted without a formal transition period through making use of the provisions of GATT Article 24 as long as the EU agreed that formal FTA talks could begin soon after March 29th. Article 24 allows countries engaged in formal free trade negotiations to suspend the

most favoured nation rule of the WTO and to continue with the existing tariff-free trade arrangements. In either case, the period would finish by December 2021 at the latest.

The EU is likely to resist consideration of this alternative for several weeks, but once the Withdrawal Agreement has sunk without trace, and both sides face no deal, there are three strong reasons why it might accept the Malthouse Compromise. First, an agreement secures the £39 billion (or more) promised in the Withdrawal Agreement. Secondly, an agreement avoids potentially high tariffs for EU exporters into the EU. The EU currently sells £55 billion of products in high-tariff food and vehicle sectors into the UK. Exports from the UK into the EU in these sectors are lower at £21 billion.

But the most pressing reason is to secure a frictionless border in Ireland. The UK has guaranteed no new border infrastructure, deal or no deal, but without a deal there will be a problem on the Irish side to maintain the integrity of the EU single market. It is obviously better for Ireland and the EU to accept some deal on the Irish border rather than no deal at all, even if that deal were inferior to the backstop in their eyes. The UK will also prefer to avoid no deal but can live with tariffs and side deals.

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