



Hogan
Lovells

Brexit

A practical response strategy



A photograph of a coastal scene. In the foreground, there's a dark, jagged rock formation. Behind it, a concrete sea wall runs horizontally. To the right of the wall, a large pile of rough, brownish-grey rocks is stacked up. The ocean is visible in the background under a pale, overcast sky. The bottom right portion of the image is covered by a dark purple, semi-transparent overlay where the text is located.

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1. Overview

Following the EU referendum in the UK, businesses around the world are assessing what impact Brexit could have on their operations and relationships in the UK, the EU, and internationally.

There are many unknowns. Acting quickly but proportionately is key to managing the risks and seizing the opportunities.

For many businesses making the best of Brexit may be the biggest strategic challenge they face in the next decade.

The key elements of a practical response strategy are:	How we can help
<p>Organize: As you would when planning for a major incident, crisis or takeover, set up a dedicated core team to develop your strategy – a “Brexit Taskforce”. This Taskforce should capture knowledge and expertise from your whole business, while ensuring strategic issues and core decision-making resulting from Brexit do not occupy all the senior team members.</p>	<p>Using our experience of working with a wide range of businesses we can help you to design a best-practice approach.</p>
<p>Inform: The potential impacts of Brexit are very wide ranging, directly or indirectly touching every aspect of business. In such a fluid and potentially confusing situation it is important that people across your business, from the Board downwards, understand the facts, have a sensible perspective on the possible implications and understand the business’ approach to the issue. A communications strategy should not only provide information and reassurance but also contribute to the process of analysis and preparation.</p>	<p>We have briefing packs both for Board level and wider engagement and can work with you to tailor these to your business.</p>
<p>Analyze: Analyze your business and the market in which you operate. Identify the potential areas of change that may arise, or which your business would like to arise, as a result of any action undertaken by the UK or EU governments while navigating Brexit. Consider all areas of your business, from sales to employee retention, to identify current or future EU initiatives which are relevant to your business and that might now change in scope or direction.</p>	<p>We have checklists which can be used to drive a program of review and analysis and can support you in implementation.</p>
<p>Capitalize: It is a cliché that business dislikes uncertainty. However, periods of turbulence and change also create opportunities. There may be opportunities to strike deals on advantageous terms, push through long planned changes or acquire assets, businesses or interests which would not otherwise be available. You should ensure that your business keeps these opportunities under review as well as the potential uncertainty.</p>	<p>Our transactional teams can provide support on a wide range of deal opportunities from M&A and real estate to key contracts and finance agreements.</p>
<p>Prepare: With the direction of travel still very uncertain, there is currently no pressing reason for business to rush into costly or radical change. However, there are some steps a business should consider taking immediately to mitigate potential risks. Looking to the longer term, you need to be ready to move quickly as soon as the shape of the post-referendum world starts to become clear and so you should begin to prepare for a range of possible outcomes.</p>	<p>Our Brexit team can involve the right technical and sector specialists to help you think the issues through.</p>
<p>Monitor: Developments remain very fluid. Over the next weeks and months your business should keep abreast of thinking in London, Brussels and in the EU Member States. It will be important to be well informed about developments – both as to the shape of the UK’s broad relationship with the EU and the very detailed specific issues which will have an impact on your business.</p>	<p>With teams across Europe, as well as in the UK and Brussels, we can help you track the latest thinking as it develops.</p>
<p>Engage: At the moment, there are many unknowns. However, whatever sector or country you operate in, the sooner you are ready to shape the impact of Brexit on your business, the greater the opportunities will be. Consider how you can most effectively engage with government to optimize the business landscape for your business, your employees and your stakeholders.</p>	<p>Our global policy advocacy team can help you to identify policy priorities and to find the most effective way to engage.</p>

2. Organize

Building an effective taskforce

The outcome of the UK's referendum will ask questions of every business over the course of a lengthy process.

These questions may be far reaching, political and even philosophical. But for business they nevertheless require practical responses. Responses which start immediately by addressing issues arising from the referendum result, but which also address the process it has triggered and the outcome of that process.

At the heart of a practical response strategy is effective organization

As you would when planning for a major incident, crisis or takeover, you should establish a dedicated core team to develop your strategy and manage its implementation. To be effective, your "Brexit Taskforce" should fulfil some fundamental requirements:

- **Broad:** Brexit will touch core regulation of products and services, organization of marketing and sales, supply chain, corporate structure, people and internal management. Your Brexit Taskforce should include representatives from key functions across your business.
- **Strategic:** Brexit will drive change: to UK and EU regulation; to trade rules; to access to a skilled work force. This change will impact you, your suppliers and customers and will raise questions going to the heart of your business. Where to trade? Who to work with? Should you change your business mix or business model? Your Brexit Taskforce should be equipped to make rapid connections between Brexit effects and your business strategy.
- **Durable:** Brexit will take years not months. Both the eventual outcome and the process to reach it are dependent on complex political and legal considerations in the UK, the EU, with other EU members and global trading partners. Your Brexit taskforce should be structured for the long-term.
- **Flexible:** Brexit will be unpredictable. The process will have twists and turns. There will be apparent lulls but issues will emerge unexpectedly and need to be dealt with quickly. Your Brexit Taskforce should have access to all the key decision makers when required whilst ensuring Brexit does not become an all-consuming distraction for your entire senior team.

- **Sensitive:** Brexit will continue to be controversial. In planning for the future your business will need to be sensitive to the concerns of both individuals and business partners who may feel exposed, and of politicians and civil servants working to find solutions which are politically deliverable as well as practical. Your Brexit Taskforce should be equipped to consider the perception as well as the substance of your business's Brexit response.
- **Opportunistic:** Brexit will create opportunities as well as challenges: to reshape the regulatory agenda; to capitalize on uncertainty of competitors, customers or suppliers; to benefit from new global trading patterns. Your Brexit Taskforce should be structured to seek out, and help your business to seize, those opportunities.
- **International:** Brexit will raise questions about the EU and other Member States – not just the UK. Should you rebalance your business toward other EU members? If the UK's departure changes the balance of EU decision making, how should you react? How will global trade with the EU evolve? Your Brexit Taskforce should be equipped to take a genuinely global view.

With an international perspective and a deep understanding of the legal, business and policy issues across a range of industry sectors and in engaging with the policy development process, Hogan Lovells can support your Brexit Taskforce in responding to and implementing legal change, and in advocating your views with the policymakers.

A practical response strategy

Organize a “Brexit Taskforce” to capture insight from across your business.

Inform your Board and wider business of the possible implications of Brexit and the approach your business is taking to it.

Analyze potential impacts or changes that your business would like to drive.

Capitalize on opportunities generated by uncertainty and change.

Prepare by taking steps to mitigate potential risks and developing a detailed plan to move quickly as clarity emerges.

Monitor developing thinking in London, Brussels and elsewhere.

Engage with government in the UK, EU and beyond, as well as with other key stakeholders.

3. Inform

Briefing internal and external stakeholders

The outcome of the referendum and the on-going political debate continues to receive significant profile. Whilst most of the practical consequences for business are currently uncertain, they are potentially significant.

In managing the effect of the referendum result and preparing for the potential next steps it is important to ensure both internal and external stakeholders are accurately informed.

This paper summarizes some of the key points to address in any communications strategy.

Why inform?

Brexit will potentially have a significant impact on any business with operations, customers or suppliers in the UK or EU. Ensuring communication of the right information and analysis (and where appropriate opinions) is therefore important for a number of reasons:

- The Brexit process could create significant risks for many businesses. Those risks may include loss of operational continuity, additional costs (for example in the form of new tariffs or the requirements of new regulatory or legal regimes), loss or redeployment of key staff and damage to supply or distribution chains. It is important that these risks are identified, scrutinized, mitigated against and progress monitored;
- Whilst there is significant uncertainty as to the details of the withdrawal process, timing and the eventual shape of the UK's relationship with the EU (and any changes to the EU itself), it is important to start preparing. This means ensuring that the range of possible outcomes is understood so that an initial assessment can be made as the potential impact on various aspects of your business and possible mitigation strategies;
- The referendum result, the political fallout and media reporting have created significant concern and uncertainty. Whilst this cannot be eliminated, it is important to ensure people have the facts, to provide reassurance where possible and appropriate, to counteract the potentially damaging impact of rumor and misinformation;
- The Brexit process is fluid and the outcome depends on the position taken by a range of players including the British Government, governments of other EU Member States and the European Commission. Issues still to be determined range from the macro (will the UK continue to have a “special relationship” with the EU) to the micro (how will very specific activities be addressed in regulation and trade). Well-informed businesses have an opportunity to try to influence the outcome in areas which matter to them; and
- Brexit is not simply a risk to business. There are also potential opportunities for business which include capitalizing on exchange rate movements, possibilities to restructure for the better, and the prospect of new UK free trade agreements with non-EU countries. A proper understanding of the landscape is important in order to understand how to take full advantage of the opportunities.

Who to talk to?

Given the breadth of the potential impacts of Brexit you should consider briefing a wide range of stakeholders including:

- The Board of Directors and key management;
- Employees and contractors (particularly those who may be personally affected by Brexit);
- Shareholders, lenders and other finance parties particularly if Brexit or the Brexit process may have a material impact on your business or create material risks;
- Industry bodies and partners with whom you may share common interests having due regard to the application of competition law, particularly when talking to competitors (See Appendix v. Trade associations and competition laws);
- Suppliers and customers who may be directly affected in ways which might indirectly affect you or who may be affected through their relationships with you; and
- Policymakers, regulators and wider opinion formers who may be able to shape the impact of Brexit and the Brexit process on your business.

Whilst the information and approach for each of these groups will vary, it is important to ensure consistency in your overall approach.

What to say?

Depending on the audience, there are a range of issues you need to consider covering including:

- The facts about what has (and has not) happened: the UK remains a member of the EU; no formal process to leave has started; no legal changes have yet happened ([Vote is Leave...the journey begins – unravelling the uncertainty](#)).
- What we know about the next steps: the only legally defined exit process (See Appendix i. Brexit — What now? Six things you need to know about the legal process of leaving the EU); possible models for the UK's future relationship with the EU (See Appendix ii. Possible models for the UK/EU relationship); the potential impact on UK law (See Appendix iii. What now? Uncoupling UK law from the EU. Further information to follow on www.hoganlovells.com/brexit);

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- Immediate issues to focus on: the risks and opportunities of uncertainty and market turbulence individuals' immigration status and business's legal obligations are currently unchanged; can existing contracts be revisited and should new contracts contain "Brexit clauses" (See Appendix iv. Brexit clauses);
- Areas of your business which could be directly or indirectly impacted and need to be assessed in preparation for possible outcomes (See section 4. Analyze: a Brexit health check): potential regulatory and legal changes; new tariff and non-tariff barriers to UK/EU trade; lost access to current EU third country free trade agreements benefitting the UK;
- Possible impacts on stakeholders and third parties, whom you may need to inform or engage on risks, provide reassurance or commence discussions to agree potential mitigations: shareholders; employees, lenders, customers, and suppliers;
- Areas of opportunity which Brexit may create for your business: new M&A and deal opportunities (See section 5. Capitalize: making the most of Brexit opportunities) and broader trade outside Europe;
- Opportunities to influence the outcome of the Brexit process or the future legal and regulatory landscape (See section 8. Engage: influencing the agenda): ensuring policymakers and regulators prioritize your areas of concern; mitigating potential change; securing optimal future policy development.



4. Analyze

A Brexit health check

The UK has not yet left the EU, or even triggered any legal exit process.

The process and timing of Brexit, and the shape of the UK's future relationship with the EU are yet to be decided but some changes are almost inevitable.

To prepare for potentially significant change, your business will need to identify the areas of potential impact. By starting that process now, your business will be in a stronger position to determine your priorities for contingency planning and restructuring.

This checklist provides a starting point for that analysis, applicable to any business. "rEU" refers to the rest of the EU excluding the UK.

1. Business scope

- ☐ Legal entities incorporated in the UK and in rEU
- ☐ Products or services provided in or to the UK and/or rEU or between them
- ☐ Internal functions provided in or from the UK and/or rEU or between them
- ☐ Products or services sourced in or from the UK and/or rEU

2. Regulation¹

- ☐ Regulatory licences/authorizations held in the UK and rEU
- ☐ Application procedures under way in UK/rEU for regulatory licences/authorizations
- ☐ Regulations applicable to current activities in the UK and rEU
- ☐ Applicable regulations which require a presence in the EU
- ☐ Time and process to obtain new approvals in the EU if required
- ☐ Key regulatory relationships in the UK or rEU which may need to be replicated
- ☐ Regulators/policymakers who may influence outcomes (including the relationship, if any, with those persons)
- ☐ Products that currently benefit from the EU mutual recognition rules
- ☐ Applicable common European standards (EU or non-EU)
- ☐ Applicable EU initiatives for new rules, regulations or standards

¹ Consider application of EU rules directly and indirectly via national legislation or regulation.

3. People

- ☐ Business dependency on people working in the UK who are rEU nationals
- ☐ Business dependency on people working in rEU who are UK nationals
- ☐ Reliance upon recognition of qualifications in rEU/UK required by employees/professions
- ☐ Continued application of acquired rights and free movement rights pending any change
- ☐ Procedures to ensure compliance with current “no discrimination” rules in employment decisions pending any change.
- ☐ Internal communications plan for Brexit related issues

4. Tax and duties

- ☐ UK/rEU payments which will no longer benefit from zero withholding tax
- ☐ Possible future reorganizations to minimize UK/rEU dividends/interest/royalties and give flexibility on later disposals and reorganizations
- ☐ Structure of planned or “in-flight” UK + rEU corporate transactions
- ☐ Potential impact of significant reduction to current UK/rEU VAT harmonization
- ☐ Potential impact of new customs duties imposed between UK and third countries
- ☐ Potential impact of customs duties imposed between UK and rEU
- ☐ Potential impact of changes to UK tax policy

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5. Trade outside the EU

- ☐ Trade flows of inputs/products imported/exported to/from non-EU countries
- ☐ Trade flows of finished products imported/exported to/from non-EU countries
- ☐ Indirect supply chain benefiting from third country free trade agreements
- ☐ Direct or indirect supply chain benefiting from EU/third country free trade agreements
- ☐ Potential impact of customs duties imposed between the UK and third countries
- ☐ Dual-use export licences held in the UK and rEU
- ☐ Application procedures under way in the UK/rEU for dual-use export licences/authorizations
- ☐ Export control and economic sanctions

6. Customers

- ☐ Customers (direct/indirect) in UK of rEU business
- ☐ Customers (direct/indirect) in rEU of UK business
- ☐ Customers (direct/indirect) in country with an EU free trade agreement

7. Contracts²

- ☐ Rights granted or received by reference to EU territory
- ☐ Exclusivity granted or received by reference to EU territory
- ☐ Contracts with termination linked to change in EU derived regulation
- ☐ Contracts with change provisions linked to change in EU derived regulation
- ☐ Contracts with “material adverse change” provisions

- ☐ Contracts involving an activity where regulation is EU derived
- ☐ Contracts with disputes clauses that assume EU conflict of laws rules apply
- ☐ Contracts and tenders related to public authorities or utilities³

8. Corporate and finance

- ☐ Shares of UK entity listed in rEU
- ☐ Shares of rEU entity listed in the UK
- ☐ Loans, bonds or financial facilities straddling UK/rEU border
- ☐ Loans, bonds or financial facilities with material adverse change clauses
- ☐ Exposure to interest rate or exchange rate/market volatility

9. Intellectual property

- ☐ EU trademarks owned, used or applied for
- ☐ IP licences granted for territories involving the UK and/or rEU

10. Data

- ☐ Activities involving collection or processing of personal data relating to individuals in the UK and/or rEU
- ☐ Employee data collected in rEU and transferred to the UK
- ☐ Customer data collected in rEU and transferred to the UK
- ☐ Employee data transferred from the UK to countries outside the EU
- ☐ Customer data transferred from the UK to countries outside the EU

² Consider existing contracts, future contracts and contract standard forms.

³ Consider existing and future contracts, terms & conditions and contract templates

11. Subsidies

- ☐ EU or UK public funding, subsidies or guarantees currently received
- ☐ Customers whose purchases are materially supported by EU or UK funding, subsidies or guarantees

12. Litigation and insolvency

- ☐ Customers/supplier relationships straddling UK and rEU where loss of automatic recognition of insolvency proceedings might impact credit assessment
- ☐ Current or planned litigation with a UK element which are based on rights derived from EU law
- ☐ Proceedings started in the UK or rEU which are based on EU free movement rights



5. Capitalize

Making the most of Brexit opportunities

The UK has voted in a referendum to leave the European Union.

The UK has not left the EU, or even triggered any legal exit process. The process and timing of Brexit, and the shape of the UK's future relationship with the EU, are yet to be decided. However, some changes are almost inevitable.

The outcome creates a number of uncertainties in the short, medium and longer term, and for many businesses is likely to increase risks and costs as a result both of that uncertainty and of change.

However, the Brexit process also creates potential opportunities. In this paper, we outline some of the areas of opportunity which businesses should explore.

Transactions

Brexit will create opportunities in the transactional market on several levels:

- The process, which is likely to involve various twists and turns, will itself have an impact on valuations and risk profiles of assets.
- We have already seen significant exchange rate movements, potentially making UK assets cheaper for overseas investors.
- Uncertainty about the outcome or potential impacts of the Brexit outcome on UK based businesses (for example, the risk that they may be at a relative competitive disadvantage) is likely to create valuation opportunities for investors who are willing to accept or manage those risks. On the other hand, with the renewed interest in UK acquisition targets, now is a good time for potential targets to review and enhance their corporate takeover defenses.
- By the same token, a shift of competitive advantage towards business located in EU countries, other than the UK, will create opportunities to acquire or invest in those businesses.
- More creatively, as the new shape of regulation emerges this may bring restructuring opportunities to enable UK businesses to continue to enjoy Single Market benefits. Those opportunities may include benefits for UK businesses in acquiring Continental European assets to create new EU operations.

Practically, businesses planning a Brexit response strategy should re-examine their historic M&A priorities and should keep opportunities under constant review as the Brexit process unfolds. In addition, business should also examine current and planned deals to identify any areas which may need to be reassessed in light of Brexit.

Our paper on Brexit and UK-related M&A (See Appendix vi) explores some of these opportunities and other implications of Brexit for transactions.

Away from M&A, the impact of Brexit provides an opportunity to review contracts and supply chains.

- Can the Brexit process be used as a legal or commercial justification for commercially advantageous change(s)? (See Appendix iv. Brexit clauses).
- For international businesses trading with the UK, are there opportunities to strike deals on favorable commercial terms in times of market turbulence or with businesses which are nervous about their future prospects, and are therefore willing to agree more favorable terms?
- For UK businesses trading internationally, can currency movements provide more competitive pricing and an attractive basis on which to secure international expansion?

Trade Deals

The UK Government has declared that its objective for a post-Brexit world is a new era of global trade.

One result of Brexit is that the UK is likely to lose the benefit of current trade deals (which are secured through the EU with third countries) and potential future deals being negotiated (such as the TTIP). This creates an imperative on the UK to seek new trade deals and, as it has already started to do, to create new trade missions.

Within the on-going EU the trade perspective will be different. One priority will be to ensure that the UK's departure does not undermine any of the EU's third party trade deals. However, Brexit will also create an opportunity to potentially simplify future trade deals by removing the UK's concerns and perspectives from those deals.

Post-Brexit, UK and other non-EU businesses which compete against EU imports may gain a competitive advantage if EU imports are subject to tariffs.

Practically, businesses should not simply monitor developments but should also consider engaging proactively with the UK Government and with the EU policymakers with a view to influencing their future trade policy priorities.

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Business Incentives

Brexit is likely to create a new climate of competition between EU Member States, other countries and major business centers.

The UK will potentially look to create incentives (including fiscal measures) to encourage business to continue their operations in the UK. This may provide EU-based businesses with the necessary impetus to restructure their operations and supply chains to ensure efficient access to the UK market.

Other EU Member States and European cities are encouraged by the very process of the fundamental review that Brexit has triggered in many businesses. The simple fact that businesses with an established UK operation are looking again at whether that is the right option, makes it a good time for those seeking to encourage investment to introduce new incentives. This means that, even if Brexit itself does not provide opportunities, new incentives introduced by EU Member States, other countries and European cities to capitalize on Brexit may create just such an opportunity – for example, non-UK businesses may want to consider relocating their UK head office to take advantage of these incentives.

Practically, businesses should examine the developing pattern of incentives and also consider the possibility of actively engaging with relevant public authorities and encouraging them to consider new patterns of incentives.

Regulation

Brexit will “shake the kaleidoscope” of regulation in the UK and in the wider EU.

Within the UK, the removal of legal requirements to align with EU regulation will create the possibility of regulatory divergence. For example, there is the possibility of influencing UK policymakers, in certain areas, to create a UK regime which is less constraining on business, or simply more attuned to the needs of businesses operating in the UK market, than the regime which applies in the EU.

In the wider EU, the removal of the UK’s influence in the policymaking process may create opportunities to redesign regulation in ways which are more fully aligned to the needs of the Single Market (and potentially the Eurozone).

Business can capitalize on this period of increased uncertainty and potential change by engaging effectively in the policy and regulatory process in the EU, EU Member States and in Brussels.

Practically, businesses should assess areas where regulatory change could create new opportunities and should actively engage early to shape the impact of Brexit on their business (See section 8. Engage).

With an understanding of all the major industry sectors, experience in every kind of corporate and commercial transaction, an experienced international trade network and regulatory and public policy expertise across all the main European markets (including the UK) as well as the Americas and Asia, our Brexit team can help you both identify and take advantage of Brexit opportunities.

6. Prepare

Tangible actions

The UK has voted in a referendum to leave the European Union but the practical consequences are currently uncertain.

The way forward is unlikely to be clear for some time; the detail may take many months or even years to determine. There could be significant consequences but, in many areas, the real impacts may be limited. Every business should be prepared for the next phase.

Three levels of preparedness

Understanding likely impacts of Brexit is an essential foundation of any Brexit preparedness strategy. Other Hogan Lovells materials explain potential outcomes to the Brexit process, and provide a checklist of areas potentially affected in your business.

Building on this, in developing your approach to preparedness you should consider the following principal elements:

- **Scenario evaluation:** understand the potential impacts of various scenarios on your business, and assess the changes you would need to implement effectively to respond to those scenarios
- **Flexibility maximization:** ensure you maximize options to respond appropriately to developments, whilst mitigating the potential risks associated with the range of foreseeable outcomes
- **Implementation planning:** plan your approach outlining the necessary changes and the practical steps required to achieve your objectives.

This paper explains how to approach each of these steps to prepare your business for Brexit.

Scenario evaluation

To understand potential scenarios and to assess the potential practical impact of those scenarios on your business, you need to evaluate the factors which will influence your business environment and the process by which change might happen.

These are:

- **Legal and regulatory change:** Brexit related changes made to your legal and regulatory environment.
- **Brexit process:** The process by which changes to the legal and regulatory environment are both determined, and take effect. In particular, any transitional arrangements which may apply.
- **Macro environment:** The manner in which both the process and substance of legal and regulatory change affect the business environment in which you operate.

Key practical point

In assessing issues in your business which Brexit might affect, do not focus solely on the obvious “front office” issues. “Back office” impacts can be just as important in practice.

In assessing potential scenarios it is important to assess these factors not simply in abstract, but also in the context of the practical reality of your business.

As with other aspects of your preparedness strategy it is important to consider every aspect of what your business does and how it operates. See Section 4 of our toolkit, *Analyze*: a Brexit health check can help you to identify the areas of potential impact.

The process should extend not simply to the “core” of your business, such as licences for your principal product or service needs, but also the broader issues which will potentially impact your business. For example: the status of employees; the regulation of consumer contracts; financial flows between UK and EU subsidiary companies.

A. Legal and regulatory change

Ultimately the impact of Brexit will be determined by the changes made to the applicable legal and regulatory environment.

One way to start to assess possible changes is to consider some of the potential “models” for the UK’s future relationship with the EU.

However, as our summary of the principal models makes clear, whilst those models help in understanding the nature of the alternatives, in practice it is likely legal and regulatory changes will be complex (See Appendix ii. Possible models for the UK/EU relationship).

From the perspective of business, each model reflects a number of possible approaches which might be taken to different types of issue. These variables include:

- divergence of UK and EU regulation
- UK approvals ceasing to benefit EU operations/sales (and vice versa)
- restrictions on movement or employment of EU nationals in the UK (and vice versa)
- imposition of tariffs on certain goods or services between the UK and EU
- the UK ceasing to participate in EU trade agreements with non-EU countries
- exclusion of the UK from EU policy development.

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Analyze potential impacts or changes that your business would like to drive.

Capitalize on opportunities generated by uncertainty and change.

Prepare by taking steps to mitigate potential risks and developing a detailed plan to move quickly as clarity emerges.

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Figure 1: Example scenario planning: template for assessing the effect of legal change

Business Issue Identified	Scenario 1 Limited Change	Scenario 2 Free Trade Agreement	Scenario 3 Full Divorce
X Licence issued by UK regulator and used for sales of product Y across the EU	Unlikely to be affected	New EU licence required; UK licence would fast track application under mutual recognition	New EU licence required – existing UK licence not recognized in EU
Movement of research team between sites in UK and Germany	Unlikely to be affected	Research staff likely to meet movement criteria under new deal if certificated	Research staff likely to meet movement criteria under new UK rules if certificated

You can only start to prepare your business for either the short or the long-term implications of legal and regulatory change if you assess the potential impact of differing legal scenarios for all of your material business issues.

You should identify each relevant aspect of your business and consider, in each case, the realistic scenarios. This will enable you to develop a template (Figure 1) and highlight particular areas of risk, opportunity and likelihood.

Key practical point

Whilst the potential for dramatic change can grab the headlines, consider whether, in practice, more subtle changes such as additional costs and bureaucracy to access the single market might be realistic scenarios for some of your business issues. In addition, the possibility of beneficial change which creates opportunities should not be overlooked.

B. Brexit process

The process by which changes to the legal and regulatory environment are both determined and take effect will, in many ways, be as significant as the eventual outcome. In particular, any transitional arrangements which may apply.

The process will be determined by:

- domestic politics (in the UK, in other EU Member States and in the EU structures);
- diplomacy (the UK, the EU institutions, other EU Member States, and other states with whom the UK or EU have trade relations); and
- practical factors (including constraints on both business and bureaucratic change such as the creation of new administrative functions).

Scenario planning for the Brexit process should consider two likely variables: timing and complexity which will apply differently to the three distinct stages of the process (see Figure 2).

Figure 2: Brexit process – key elements



Some basic process scenarios to consider are:

- “Quick fix”: rapid political agreement on a “limited change” way forward
- “Gunpoint Divorce”: politics drives a rapid exit without adequate preparation
- “Marathon chess”: every issue is addressed and resolved taking many years
- “Ill-prepared”: long but confused negotiation badly implemented
- “Infinite horizon”: decisions blocked by political or constitutional gridlock creating an indefinite process.

Each of these alternatives would have different potential implications for the approach to a range of business issues.

Key practical points

Scenario planning the impacts of the Brexit process are as important as planning for the outcomes of that process.

The outputs of your scenario planning exercise should be combined in a consolidated risk register (see Figure 3).

C. Business environment

The Brexit process, the substance of legal and regulatory changes and perceptions of each of those factors will influence the environment in which your business operates.

Immediately following the referendum results, there were significant fluctuations in both the UK’s and the EU’s exchange rates. You should anticipate the possibility of further turbulence and changes in business sentiment and environment.

Relevant effects may occur on a macro level (such as exchange rate movements) and on a micro level (for example, instability amongst suppliers of particular industries if it is perceived that the industry will be damaged by Brexit).

Your scenario planning should assess areas where relevant changes in the environment:

- are foreseeable as potential consequences of the Brexit process or outcome; and
- if they materialized would create material business risk or opportunity.

Figure 3: Consolidated scenario planning risk register

Business Issue Identified	Risk/ Opportunity	Scenario in which it is likely to arise	Severity (H/M/L)	Actions to mitigate or take advantage	Responsibility
Legal/regulatory change					
Brexit process					
Business environment					

Maximizing flexibility

In the absence of clear evidence that any particular change will take place in the foreseeable future, the possibility of Brexit related change is a “known unknown”.

In that sense the Brexit referendum result is only a particularly significant example of a much wider category of uncertainty.

For example, the 15 months starting with November 2016 see elections in the U.S.A., France, Germany and Italy. Any one of these events could result in the election of an administration committed to fundamental change in domestic and/or international policy, with potential impacts on particular business activities which might equal, or even exceed, those of Brexit.

This means that, in the absence of other factors, taking drastic action whilst the Brexit outcome remains uncertain will, for many businesses, be irrational. Assuming that there are good reasons under current regulatory and trading regimes to operate in a particular way, there is currently no more certainty that those reasons will cease to be persuasive than there is that the political, legal or regulatory environment in any other major economy might change radically.

Equally, it is entirely conceivable that the Brexit process may create new opportunities. To take one example, the UK Government might offer significant fiscal incentives to international businesses to maintain a UK presence in order to offset any adverse consequences of Brexit.

More broadly, Brexit is a symptom of a generally heightened climate of economic and geopolitical uncertainty. So, whilst there may be circumstances in which immediate change might be appropriate, the level of uncertainty surrounding Brexit and broader factors means that, for business, maintaining appropriate flexibility, to respond to both emerging threats and opportunities, will be the single most important current step available to prepare.

- **Deferring action:** delaying legal commitments or expenditure pending further clarity. Whilst this may be achieved by simply holding off action, also consider whether agreements can be structured to include conditions which allow you to manage the level of commitment you are making (e.g. capital investment).
- **Securing options:** taking steps which will make it easier to follow a range of risk management strategies going forward. For example, it is unlikely to be appropriate to relocate activities from the UK to another EU Member State at this stage. However, ensuring that you have sufficient legal and practical presence and regulatory relationships in at least one EU Member State, other than the UK, would make it easier to react quickly to future developments.
- **Avoiding lock-In:** structuring arrangements in a manner which provides an ability to change course if necessary. This can involve inclusion of a so called “Brexit clause” (See Appendix iv. Brexit clauses) or simply limiting the duration or scope of commitments (for example, keeping the term of contracts shorter, avoiding exclusivity commitments or limiting volume commitments under them).

Key practical points

Managing risk is inevitably expensive so it is important to keep Brexit related risks under constant review to ensure risk management strategies have an appropriate cost benefit profile.

As Brexit is only one of a number of geopolitical risks and may not eventually prove to be the most significant, maintaining flexibility is likely to be a more appropriate response than making immediate fundamental change.

- **Spreading risk:** taking commercial steps to mitigate exposure to any specific risk. This might include, for example, explicit hedging of exchange rate or commodity price risk. However, it might in addition extend to making changes to your internal structures, supply chain or sales or distribution networks in such a way as to balance exposure to Brexit related risks with other potential risks.

For example, going forward a U.S. company looking to establish a European sales network might be well advised to appoint distributors in the UK and in another EU country, rather than routing all sales through a UK-based partner.

Inevitably many of these risk management strategies are likely to carry a cost. This emphasizes the fact that a priority for a preparedness strategy is to keep the profile of Brexit risks under constant review, so that the use of these potential costly strategies is appropriately balanced with the developing risks.

Implementation planning

Having identified potential Brexit impacts and taken steps to preserve flexibility, you should also develop plans to implement change as and when the position clarifies.

The precise nature of plans will be different for every business. However, plans might typically include:

- **Regulatory restructuring:** Some outcomes may mean that the requirements of EU and/or UK regulation may require that you locate certain functions within their territory in order to continue to operate your business in its current form.

Practical points to plan for include:

- Should functions transfer from the UK to another EU member (or vice versa) or do they need to be replicated in both?
- Is it better to limit the scope of restructuring to the minimum achievable or will that generate excessive complexity?
- Are there alternatives to replication or transfer which would allow your business to continue substantially unchanged? For example, working in partnership with another entity which already has the necessary presence.

- Would changing the scope of your activities be a more appropriate response? For example, should you consider selling businesses in either the UK or other EU Member States to another business which is better placed to operate in the new regulatory environment?
- How would restructuring or replication affect the tax efficiency and transfer pricing model used for your business?
- What is the most appropriate legal structure by which to implement the transfer? Primary options to consider include business and share sale and, whilst the UK is an EU Member cross-border merger and transfer using Societas Europea. Specific additional considerations are relevant in particular industries including financial services.
- What are the principal practical challenges of change? What constraints, costs and procedures need to be followed from the perspective of employment law? Are you constrained by contracts?
- **Business restructuring:** Some outcomes may mean that, even in the absence of a direct regulatory requirement, the business impacts are such that your existing business structures are no longer optimal. Reasons for this might include the additional costs associated with a post-Brexit world or tax inefficiencies of current structures.

Key practical point

In shaping implementation plans, consider: What is the reasonable range of potential outcomes to plan for? How far to progress planning for a range of alternative scenarios? When should implementation of the plan start?

Practical points to consider in developing an implementation plan in this context will have many similarities to those applicable to regulatory restructuring but inevitably there will be greater flexibility in determining the approach:

- **Regulatory compliance:** Some outcomes may mean that regulation in the UK diverges from that in the EU. These outcomes are also likely to see an enhanced role for UK regulators and policymakers in areas which are currently primarily driven at an EU level.

Practical points to plan for include:

- establishing a process to review compliance at the point regulatory change occurs taking account of the fact that this will, potentially be a time of intense change when there will be significant pressures on your internal and external compliance resources
- establishing new compliance capabilities which will be capable of managing compliance, regulatory relations and policy development in both the UK and EU markets going forward, taking account of the fact that regulatory expertise is likely to be at a premium.
- **Contracts:** Some outcomes may mean that existing contracts no longer function as originally envisaged or that contract provisions (whether in your favor or in favor of a contract counterparty) are triggered. In addition, regulatory change (see above) may necessitate changes to either existing contracts or future use of standard terms and conditions or other standard contracts:

Practical points to plan for include:

- reviewing existing contracts for areas of particular risk. These are likely to include:
 - provisions defining territory by reference to the EU
 - provisions built on the assumption of a single market (e.g. applying English law to consumer contracts for consumers across the EU)
 - force majeure/material adverse change clauses
 - dispute resolution clauses that choose litigation rather than arbitration

Key practical points

As its most basic a “full Brexit” would create two new markets (the UK and the EU) where today one exists, As the UK is more than 15% of the total EU economy and is one of the six biggest global markets, any Brexit driven change needs to contemplate the need to serve both the EU and the UK going forward.

At the point when the need for new regulatory capabilities becomes clear, there will be significant pressure on both your internal capabilities and the availability of external compliance resources.

- provisions dealing with pricing which might constrain your ability to pass on additional Brexit-related costs or allow a counterparty to pass those costs on to you.
- reviewing contract templates and contracting mechanics particularly for pan-European consumer activity (e.g. eCommerce).
- **Supply chain:** Some outcomes may have indirect impacts through their effect on parties in your supply chain.

Practical points to plan for include:

- the possibility of changing the profile of your supplier base as a way of managing risk
- the possibility of increased risk of financial distress in your supplier chain which you may be unable to directly influence
- will business throughout your supply chain be as well prepared as you to address regulatory and other Brexit-related change?



7. Monitor

Providing informed insight

Brexit means different things to different businesses. The implications will depend on the sector in which you operate, the nature of your product or service, the profile of your investments, suppliers and customers, and how you view the balance between the opportunity to expand, and the risk to your ability to continue, your commercial activity.

The general uncertainty about future arrangements in trade, regulation and the broader UK-EU relationship extends across all sectors. It is important to approach this uncertainty fully prepared and aware of all potential ramifications of Brexit on all relevant areas of your company's operations; this requires the gathering of political and commercial intelligence which can be interpreted to secure informed insight.

Knowledge is power

While developments remain fluid politically and economically, it is important to ensure that your business is aware of:

- shifts in the political landscape in the UK and the EU;
- developments in legal and regulatory thinking; and
- how these are being viewed in markets further afield.

Over the next few months and years your business should remain abreast of developments in London, Brussels and the other EU Member States. Key to this will be optimizing the ways in which you gain your intelligence and insight. You should be well informed about public developments. However, it is equally important to gain an understanding of the underlying pressures, motivations, conflicts and issues in relation to the UK-EU relationship, and the complex issues which will have a practical impact on your business.

Why this is important to your business

The outcome of individual components of the Brexit process on your business will be influenced and determined by a host of factors.

By taking the opportunity to plan ahead and remain informed on the ongoing political and economic situation across the UK and all Member States, a process which will require consistent review and refinement, you will be able to actively educate decision-makers and influence policy by building arguments that support your strategic business-critical objectives.

More than “skin deep”

Knowing what someone is saying is easy. The more important, and difficult, thing is working out why they are saying it and what can be done to change or neutralize it. Government and executive decisions can be driven by political dogma but logical arguments, facts, evidence and a wider constituency of support can also shift opinions. Three valuable contributions to this are:

- awareness of consensus on issues that impact on your sector but are relevant to others;
- knowing what trade-offs can be secured during negotiations;
- effective monitoring and critical assessment of available knowledge.

How we can help

Hogan Lovells has a dedicated team which will track regulation, legislation and legal changes in order to provide detailed information to you. This is augmented by our professional library services that monitor developments and provide real-time updates.

We will use intelligence from long-held contacts – including officials and politicians in the UK Government and Parliament, the European Commission, Parliament and Council, and in national capitals – and other opinion formers, commentators, media networks and think tanks, as well as monitoring “as-it-happens” news, views and information sourced from social media, traditional news feeds, speeches and events.

This combined intelligence is then assessed by our teams so that we are able to provide commercial and political intelligence and insight to support the development and implementation of your company’s engagement and legal strategy.

A practical response strategy

Organize a “Brexit Taskforce” to capture insight from across your business.

Inform your Board and wider business of the possible implications of Brexit and the approach your business is taking to it.

Analyze potential impacts or changes that your business would like to drive.

Capitalize on opportunities generated by uncertainty and change.

Prepare by taking steps to mitigate potential risks and developing a detailed plan to move quickly as clarity emerges.

Monitor developing thinking in London, Brussels and elsewhere.

Engage with government in the UK, EU and beyond, as well as with other key stakeholders.

8. Engage

Influencing the agenda

Following the EU referendum in the UK, businesses around the world are assessing what impact Brexit could have on their operations and relationships in the UK, the EU, and internationally.

At the moment, there are many unknowns. However, whatever sector or country you operate in, the sooner you are ready to engage with government to shape the impact of Brexit on your business, the greater the opportunities will be.

The following policy engagement steps will help you to optimize the business landscape for your business, your employees and your stakeholders.

- 1. Set up an internal “Brexit Taskforce”:** Include any internal public affairs specialists in your Brexit Taskforce, and ensure that government engagement is placed within the Brexit Taskforce’s remit.
- 2. Analyze:** As part of its analysis of your business and the market, your Brexit Taskforce should identify the potential areas of change that may arise, or which your business would like to arise, as a result of any action undertaken by the UK or EU governments while navigating Brexit.
- 3. Evaluate and focus:** Once you have a detailed picture of all potential impacts (positive and negative), identify those issues that are business-critical. Some will be “big picture”, such as whether the UK remains in the single market, and some will be more specific to your industry and business. Your Board and Brexit Taskforce must then focus on the priority areas and not get distracted by those that are less critical.
- 4. Appoint advisors:** Identify suitable external advisors to work with you to develop and deliver your strategy. They should have expertise in intelligence gathering, and be able to act as credible negotiators on your behalf in the UK, Brussels, other major EU Member States and internationally. Bear in mind that the decision-making processes in the UK and at an EU level will take place in a complex competitive environment: the most credible and informed voices will have a better chance of being heard.
- 5. Be ready to engage:** Along with your external advisors, develop clear legal and commercial arguments as to why your objectives should be taken into account in Brexit negotiations and arrangements. The UK government has stated that it will listen to sound economic, social and commercial representations from the business community, and that every business should seriously seek to engage in a constructive and pragmatic manner. The European Commission will be no different, and EU Member States are already actively listening to their industries to shape the roadmap for the Brexit negotiations.
- 6. Articulate your response:** Develop clear briefing materials. These should make constructive suggestions as to the optimum outcome for your business and should include the arguments that support your strategy, as well as countering any known strategies of competitors. Keep your messages consistent. Consider how you might broadcast your views to a wider audience (or persuade others to do so) by publication of articles in newspapers, journals, social and other media.

- 7. Find allies:** Your business needs may be very similar to those of other companies in the UK, EU and beyond. Look for like-minded thinkers with common ambitions. If appropriate, build new contacts and coalitions. If you are a member of a trade association, make sure you get your voice heard (See Appendix v. Trade associations and competition law). Seek out well-respected third parties who might support your negotiations and help you to have a strong say in Whitehall, the Berlaymont, and EU Member State capitals, as well as through influential media.
- 8. Identify targets:** Identify the key political stakeholders and influencers with whom your business must engage. Mapping the relevant officials and departments is a vital preparation process for effective and strategic engagement, and this information should be kept up-to-date. It is also important to remember that some EU Member States will have strong views on the future of certain sectors, and there may well be value in engaging with their governments too.
- 9. Be constructive:** As you start to engage with the UK government, EU Member States and the EU, consider carefully how your business can assist at this challenging time – what can you offer to help them navigate uncharted waters and to secure the best deal?
- 10. Stay ahead:** As more clarity starts to emerge, continue to tailor and develop your strategy. Be ready to influence any future trade deals with third countries when negotiations commence, and to do so on both sides of the discussion. It is never too early to build up your international contacts base, focusing on your business's key markets.

Planning for Brexit is likely to be the biggest strategic challenge for many businesses in the next decade. Our dedicated Brexit service combines experienced, sector-focused legal counsel with political monitoring and government, stakeholder and media relations advisors.

We can help you to analyze your current environment; develop a strategy for shaping the law, regulations and arrangements that most affect your business; work alongside you to engage and negotiate with the right decision-makers in government using the most persuasive arguments; and advise you on the business impact of each development as it happens.

A practical response strategy

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Inform your Board and wider business of the possible implications of Brexit and the approach your business is taking to it.

Analyze potential impacts or changes that your business would like to drive.

Capitalize on opportunities generated by uncertainty and change.

Prepare by taking steps to mitigate potential risks and developing a detailed plan to move quickly as clarity emerges.

Monitor developing thinking in London, Brussels and elsewhere.

Engage with government in the UK, EU and beyond, as well as with other key stakeholders.

9. Making the best of the post-referendum world

Businesses around the world are assessing the potential impact of Brexit on their operations and relationships in the UK, the EU, and internationally, and on the commercial and investment opportunities open to them.

For many businesses, making the best of Brexit may be the biggest strategic challenge they face in the next decade.

The Hogan Lovells solution: creative solutions to extraordinary challenges

Working at the intersection of business, government, politics and law, we provide an integrated solution that combines legal excellence and global, cross-sectoral experience with political intelligence, professional advocacy and strategic government relations.

Our dedicated Brexit service brings together experienced, sector-focused legal and international trade counsel with government, stakeholder and media relations capability supported by expert monitoring and interpretation.



To our deep sectoral and local understanding we add the international and cross-sectoral breadth that allows us to see across the issues. That means we can deliver creative solutions and coordinated strategies to meet extraordinary challenges and to make the most of emerging opportunities.

Organize

Brexit has the potential to touch every part of every business which involves, directly or indirectly, the UK or EU. Business needs to have a structured approach which involves every business function without swamping them.

What we do

We can help you create the right Brexit Taskforce and structure the right management, board and shareholder briefings.

We can help you to work with other interested parties without transgressing competition law.

Inform

Ensuring communication of the right information and analysis (and where appropriate opinions) is important given the potential risks and opportunities and the need to reassure and to plan.

What we do

We can help you prepare briefings for internal and external stakeholders.

We can help you to explain the complexities of the interaction of UK and EU law and how they might be separated.

Our industry specialists can help in shaping the key messages outlined in this paper to your sector.

Analyze

The impact of the UK's exit from the EU is wide-ranging directly and indirectly touching many aspects of your business, in the UK and elsewhere. The political and trading environment is fluid, but your business-critical issues are not.

What we do

We will work to understand your business needs and priorities, to assess where change is most likely to affect you, and to identify opportunities and challenges that might result from future policy shifts.

We will help you to establish why and to what end you should seek to influence the legal, regulatory and trade policy choices being made, and where your priorities lie.

A practical response strategy

Organize a “Brexit Taskforce” to capture insight from across your business.

Inform your Board and wider business of the possible implications of Brexit and the approach your business is taking to it.

Analyze potential impacts or changes that your business would like to drive.

Capitalize on opportunities generated by uncertainty and change.

Prepare by taking steps to mitigate potential risks and developing a detailed plan to move quickly as clarity emerges.

Monitor developing thinking in London, Brussels and elsewhere.

Engage with government in the UK, EU and beyond, as well as with other key stakeholders.



Capitalize

Brexit creates opportunities as well as threats: to take advantage of uncertainty; to reshape the business environment; to restructure and reappraise your business.

What we do

We can help you identify opportunities – in contracts, in acquisitions, in restructuring, in the regulatory environment.

Our transactional, regulatory and public policy teams can execute change.

Prepare

Your business needs not simply to understand the potential implications of Brexit but also to take concrete steps to maximize flexibility, to respond to the uncertainty and plan, how to implement necessary change.

What we do

We can help you understand the scenarios which you might face and assess the right plans.

We can identify where you need to preserve flexibility and how to make legal arrangements which achieve that.

We can devise the right business structures and the optimal approach to compliance in a post-Brexit world.

Monitor

Brexit is a process not a single event. It will be a process of change not simply in the UK's relationship with the EU but also policy and regulation within the UK, EU and Member States. Understanding that process as it unfolds will be critical to successfully addressing the Brexit challenges.

What we do

We will track political, sectoral and industry sentiment to support on-going programs. We will use intelligence sourced from long-held contacts — including officials and politicians in the UK Government and Parliament, the European Commission, Parliament and Council, and in national capitals — and other opinion-formers, commentators, media networks and think-tanks, as well as monitoring real-time news, views and information sourced from social media, traditional news feeds, speeches and events.

We will use this intelligence to provide trend analysis, commentary and insights that support the development and implementation of your strategy.

Engage

Brexit will create a window of change. The direction of that change will not be determined in a vacuum but in the context of legislators' and regulators' perspectives. Your business can help to contribute to those perspectives but only if you actively engage.

What we do

We will use our legal, commercial and policy knowledge and political intelligence to deploy effective written material, direct representations, third-party endorsements, speech platforms, media engagement, social media and web presence, to help to secure the policy decisions that meet your business objectives.

We will work alongside your own teams and other advisors to engage with key stakeholders, using the most appropriate legal and policy arguments as well as proven communication techniques in a carefully coordinated and choreographed program.

Appendices





Appendix i

Brexit – what now? Six things you need to know about the legal process of leaving the EU

The political implications of the referendum result have been seismic and sudden, both domestically and internationally.

However, legally speaking, the referendum result has no immediate effect. It is only advisory in nature. The UK continues to be a member of the EU today. As a matter of EU law, it is still bound by the EU Treaties and subject to the jurisdiction of the Court of Justice of the European Union. And as a matter of UK law, the European Communities Act 1972 — which gives domestic legal effect to the UK's membership of the EU, including giving EU law precedence over UK law in the UK courts — remains in force.

Although there has been some suggestion of UK legislation prior to Brexit to limit the jurisdiction of the European Courts (among other things), the UK's legal relationship with the EU will not change until the UK formally withdraws from the EU. The only legal mechanism for withdrawal is that set out in Article 50 of the Treaty on the European Union ("TEU"). This requires the UK to issue a formal notice to the European Council (the Heads of State and Governments of the EU Member States). There is no mechanism for the EU (or remaining Member States) to expel the UK or suspend its membership.

The ordinary treaty revision procedure and the provisions for the accession of new Member States might also become relevant in the event of an initiative for an independent Scotland to remain with the EU. However, for the UK to withdraw using any other mechanism would require unanimous agreement among the remaining 27 Member States of the EU.

In practice, it is likely that the UK's exit will be a matter of political negotiation and to that extent the formal Article 50 procedure may be invoked only if, and in the manner that, it is seen as helpful in the context of those negotiations.

So what does the Article 50 TEU process look like? Here are six things to know:

1. When does the UK have to notify the EU of its decision to leave?

While there is undoubtedly a political imperative, the UK Government has no domestic legal obligation to commence the Brexit process by any date (or at all). Under EU law, notification pursuant to Article 50 is unilateral. It is up to the UK when it notifies the European Council of its decision to leave; no timeframe for notification is provided under Article 50. The EU has indicated that the Article 50 notice can be served in writing, or orally at a meeting of the Council and noted in the formal minutes.

Article 50 provides that a member state can decide to withdraw from the EU "in accordance with its own constitutional requirements". As a matter of UK constitutional law, the act of triggering Article 50 is an exercise of the royal prerogative, a collection of powers held by the UK Government on behalf of the Crown. It is therefore a matter of discretion for the Prime Minister when to invoke Article 50. However, as pointed out by Sir Paul Jenkins KCB QC (former head of the UK Government Legal Service from 2006-2014) in an [opinion](#) published on 26 June 2016, the exercise of the royal prerogative in these circumstances may be subject to the constitutional convention, known as the Ponsonby Rule, that government proposals for international acts (such as major Treaty change) are brought before Parliament and debated before any formal executive action is undertaken. Others have [suggested](#) that the Prime Minister cannot exercise the prerogative without parliamentary approval.

The UK may wish to delay formal notification to allow time for informal initial negotiations with Member States to take place outside the formal timeframe. Prime Minister David Cameron has indicated that this will be a matter for his successor, so we can expect notification not to be given until October 2016, at the earliest, and the UK Government may wish to create as much breathing space as possible before the process kicks off. However, the remaining 27 Member States, the European Commission and the European Parliament may not be prepared to engage in informal negotiations until notice has been given and the UK can expect to come under growing pressure to serve notice sooner.

2. How would the withdrawal negotiations work?

By contrast to notification, the act of withdrawal from the EU is not unilateral: once notification is given, the process is determined by the procedure set out in Article 50 TEU, which provides for the negotiation of a withdrawal agreement between the withdrawing Member State and the EU.

Once the UK gives formal notification of its intention to leave and the Article 50 TEU process is commenced, the countdown to Brexit begins in earnest. This period can only be extended by a unanimous decision of the European Council. Depending on the progress and content of negotiations, it is possible that other Member States could threaten to veto a possible extension in order to strengthen their own bargaining position.

As to the conduct of the negotiation process itself, under Article 50 TEU, the European Council, after having received a recommendation from the European Commission, will first adopt a decision authorizing the opening of negotiations and nominating a head of the EU negotiating team. Conduct of the negotiations will be the responsibility of the Commission negotiation team, but is likely to be closely overseen by the European Council

and subject to informal comment by the European Parliament throughout the process.

The withdrawal agreement is subject to specific procedures different from those used, for example, for trade agreements. Once the negotiations are complete, the European Parliament must consent to the draft withdrawal agreement by a majority of votes, after which it is signed and concluded by the Council (if agreed by Qualified Majority Voting, which effectively amounts to 20 out of the 27 remaining Member States, representing 65% of the total population of the EU). If the withdrawal agreement is a “mixed” agreement, in that it engages Member State as well as EU competences, it will also need to be ratified by each of the remaining Member States as well.

Can the UK change its mind? Article 50 TEU does not make provision for the UK to retract its notification once given. On its face, the ultimate effect of the notification (that is, termination of membership) is automatic. However, it is likely that retraction would be legally possible, at least if the political will existed. However, the political implications of doing so would be significant for the UK’s future status in the EU, and it might require the consent of the remaining 27 Member States – especially if the retraction takes place after conclusion of the withdrawal agreement. However, once the withdrawal agreement takes effect, the UK will have left and there would be no going back.

In the event that the withdrawal agreement takes effect such that the UK leaves the EU and the UK subsequently decides that it wishes to re-join, any request to re-join the EU would be subject to the procedure outlined in Article 49 TEU, in the same way as a new applicant. As such, it is entirely plausible that the EU, as part of any accession negotiation, might be unwilling to permit the UK to opt out of certain policy areas as it does currently, such as in relation to the Schengen Area or the euro.

3. What will the negotiations cover?

Article 50 TEU provides that the EU will negotiate an agreement “setting out the arrangements for its withdrawal, taking account of the framework for its future relationship with the Union”. The content and scope of the withdrawal agreement is not defined by Article 50 TEU and will not become clear until the nature of the UK’s future relationship emerges in the early stages of the negotiations. It is therefore not clear whether the future relationship of the UK with the EU will be covered by the terms of the withdrawal agreement or negotiated as a separate agreement. At a minimum, the withdrawal agreement will need to take account of the framework for the UK’s future relationship and provide for transitional provisions, where necessary.

If the terms of the UK’s future relationship are negotiated as a separate agreement, this could be an Association Agreement under EU law, entered into by the UK, the EU and the remaining Member States and requiring unanimity in the European Council and consent of the European Parliament.

In addition to its negotiation with the EU in relation to withdrawal and future relationship, the UK will also need to negotiate Free Trade Agreements with non-EU states that have such deals with the EU. It is possible that these negotiations could take place at the same time at the EU negotiations. However it is more likely that non-EU states would be reluctant to agree to anything until they knew what the UK’s future relationship with the EU would look like.

4. Can the negotiations realistically be completed within the period specified by Article 50 TEU and what are the consequences if no agreement is reached?

It is unclear at this stage whether negotiating the UK’s withdrawal is achievable within the two year period under Article 50 TEU. The UK Government has stated that “due to the complexity of the negotiations” it would be difficult to complete the negotiations before the two year deadline. However, there is likely to be pressure to complete negotiations before the current term of the European Parliament and European Commission ends in 2019. Such time pressure might itself lead to the UK’s withdrawal being separated from the negotiation of the definitive replacement arrangements. It may be that a provisional regime would be put in place while the latter negotiations are completed.

If the UK were to reach the end of the two year period specified by Article 50 TEU without having reached an agreement, and if one or more of the 27 other Member States vetoed an extension of this period, the UK would leave the EU automatically, without a replacement agreement in place. In these circumstances, the UK would cease to have access to the single market and would no longer benefit from its current trade relationship with the EU, nor the free trade agreements from which the UK benefits by virtue of its EU membership. The UK’s trade relations would instead rely on the default position under applicable World Trade Organisation rules until new agreements could be reached.

5. How will the withdrawal negotiations affect the UK’s continuing participation in the EU prior to withdrawal taking effect?

During the negotiation period, the UK’s position and influence within the EU will undoubtedly be affected by its pending departure. While the UK would remain a full member of the EU over the course of the negotiations, its credibility as an active member would be undermined and its ability to affect EU decision making would be lessened. The resignation of Lord Hill as Member of the European Commission on 25 June is indicative of the immediate impact on the UK’s involvement in EU decision-making.

In particular, the UK is scheduled to hold the presidency of the European Council from July to December 2017. Triggering Article 50 TEU would mean that the UK would be disqualified from participating in European Council meetings on the negotiation of the UK’s withdrawal, a matter that is likely to be a key concern of the European Council during this period. As a result, the Chairman of the House of Lords EU Committee has already urged the UK and EU to seek alternative arrangements “as a matter of urgency”.

6. Can the UK seek to disapply aspects of its EU membership before formally withdrawing?

Some in the Vote Leave campaign have suggested that the UK could alter its relationship with the EU unilaterally before the withdrawal agreement takes effect by amending domestic legislation that incorporates EU law into UK law. Such legislative changes could include, for example, amending the European Communities Act 1972 so as to unilaterally allow the Government to remove EU citizens whose presence is deemed not conducive to the public good, provide that the EU Charter of Fundamental Rights does not prevail over UK law, or restrict recognition of rulings of the Court of Justice of the EU in national security matters.

Any such move unilaterally to disapply aspects of the UK's EU membership before it has negotiated the terms of its withdrawal from the EU could have unpredictable results. In particular, it is not clear how UK judges would respond to conflicting demands from UK and EU law while the UK is still a Member State of the EU. Paradoxically, any such legislation would be susceptible to legal challenge on the basis that it is incompatible with EU law but for any provision in it precluding such a challenge. This would be likely to give rise to litigation and legal uncertainty one way or another.

How can we help?

Analysis, Tools, Monitoring, Implementation

We have conducted an in-depth analysis of how Brexit could affect different industry sectors and worked with a range of clients to develop their contingency planning. We understand the range of issues and responses. We can guide you on how to optimize your business position. As the legal landscape emerges from the referendum fog, we can alert you to relevant developments and advise on navigating the new opportunities and challenges it will deliver.

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Appendix ii

Possible models for the UK/EU relationship

This paper summarizes some potential alternative models for the UK's future relationship with the European Union, together with the key differences between the models which will need to be addressed in determining both the shape and impact of that new relationship.

The purpose of this paper is to enable business to understand the principle features of the potential outcomes to the political process underway, rather than to address specific issues, of which there are many, in detail.

In this note you will find:

- A summary of the key features of the UK's current membership of the EU;
- Four potential alternative models for the UK's future relationship with the EU, together with their key features;
- An overview comparison of each of the four potential alternative models.

Known-unknowns

This process is political as well as legal, and so we have not attempted to assess the probability of any outcome, instead we have tried to describe some of the possible factors and areas of potential trade off in the political process.

A “pick and mix” solution?

As we describe in the final section of this note, although various “models” are helpful in understanding the spectrum of possibilities, it is quite probable that the eventual outcomes, whilst lying somewhere on this spectrum, will not precisely reflect any of these models but a “pick and mix” combination of elements from them.

Current model: EU membership

Background

The EU creates a framework through which the UK and 27 other Member States cooperate. At its core is the principle that the combined territory of those states form a Single Market within which goods, services, capital and people can move freely, there is fair competition and consumers and workers are protected. The fundamental principle is that EU citizens must not be discriminated against on the grounds of their nationality, including in relation to free movement.

The rules are set out in EU law which exists in parallel with the laws of the individual Member States. The EU has its own legal personality and institutions through which legislation is enacted, executive decisions are made and EU law disputes determined. The EU also has a series of areas in which it has exclusive competence such as trade matters (including a common external tariff on imports from outside the EU) and negotiates arrangements with external countries in areas such as trade.

Whilst the EU is responsible for the rules governing large areas of economic activity (with the aim of ensuring a common approach throughout the EU territory), these rules are, in many cases, implemented in some part via the institutions and laws of individual Member States as well as via EU law. In addition, the EU has no role or a limited role in many areas of law (including much of that governing contracts, companies and real estate) or in relation to direct taxation.

Key features

The relationships between the UK, the EU, other Member States and countries outside the EU have expanded into a complex network within the world trading system. However, in comparing various models, some key aspects can be summarized as follows:

- **Single market:** Goods, services, people and capital can move freely within the EU. This has several notable features:
 - **No tariffs:** no tariffs are imposed on trade within the EU but there are common tariffs on imports to the EU;
 - **Common standards:** goods and services fulfilling EU-based rules or standards in one Member State automatically comply with the equivalent rules or standards EU wide. In many areas, country-by-country compliance is not required;
 - **Regulatory passport:** where provision of goods or services requires an EU derived regulatory authorisation, an entity established and authorised in one Member State satisfies equivalent requirements throughout the EU. In many areas country-by-country authorisation is not required;
 - **Trade agreements:** the EU negotiates and concludes trade agreements with non-EU states for the benefit of all Member States; and
 - **Movement of People:** Citizens of any EU Member State are free to travel, work and study throughout the EU;
- **Influence:** The UK has the right to participate in EU decision-making (and so influence EU policy and law), other than in the areas from which the UK has opted-out;
- **Law:** EU law (which, in the areas where the EU has a role, extends from fundamental principles to detailed regulation) applies to, and within, the UK, except in the areas of the UK's opt-outs; and
- **Contribution:** The UK makes a financial contribution to the EU budget¹ on the basis of its GDP.

Opt-outs

The UK (and some other Member States) has, by agreement, opted out of various aspects of the EU's operation. In the UK's case these include opt-outs from membership of the single currency (the Euro), Banking Union, and the Schengen Agreement (which removes border controls between certain Member States).

¹ The calculation of the UK's contribution is complex as, in practice, a significant amount of the headline figure is credited back to the UK Government

Alternative 1: New terms model

Background

The UK’s referendum is consultative and does not commit the UK to leaving the EU.

With political developments in the UK and the EU currently being extremely fluid and the likelihood that any process to finalize the UK’s departure will take several years, it is possible that the outcome of the political process is that the UK remains a member of the EU.

However, it is likely that this scenario would also involve changes to terms of the UK’s membership to address the key concerns raised by the “Leave” side in the referendum campaign; in particular, unrestricted freedom of movement of people and the size of the UK’s financial contribution to the EU budget.

A further unknown in this scenario would be whether any changes are limited to the UK’s terms of membership or would take effect as more wide-ranging changes to the EU, i.e. affecting all Member States.

Key features

The essence of this model is that the status quo would remain largely unchanged, subject to specific additional qualifications or opt-outs. The UK would continue to enjoy the benefits of being a full member of the EU and be subject to the common legal, political and economic commitments required of all EU members.

New terms model: Summary	
No tariffs	No change
Common standards	No change
Regulatory passport	No change
Trade agreements	No change
Movement of people	Additional restrictions?
Influence	No change
Law	No change
Contribution	Possible reduction

Formal requirements

New terms would need to be agreed by all of the other 27 Member States.

Implications for business

This model would provide business with a high degree of stability. Any changes to the principle of the free movement of people would be unlikely to affect highly skilled workers being recruited for specialist or management positions or the relocation of existing employees. However, restrictions could potentially increase administration and associated costs, and might make it more difficult to recruit candidates for less skilled roles.

Alternative 2: EEA model

Background

Norway, Iceland and Liechtenstein are all members of EFTA and the EEA.

The UK was a leading player in the creation of EFTA in 1960 as a free trade driven alternative to the EU, which was seen as being too focused on political integration. In the following years, EFTA membership has declined as most of its members, including the UK, have left to join the EU.

The EEA model assumes that the UK, like Norway, is a member of both the EEA and EFTA. Switzerland, a member of EFTA but not the EEA, is a special case raising issues which have similarities to those facing the UK (see “Overview of Models and Possible Outcomes” overleaf).

Key features

Membership of the EEA provides access to the Single Market (whereas EFTA membership alone does not) but outside the structures of the EU. EU law does not apply directly within the members of the EEA.

However, in areas relevant to the Single Market, EEA Member States are obliged to adopt laws equivalent to those of the EU. EEA members have a limited veto right, the exercise of which could result in suspension of membership of the Single Market. In practice, in those areas the UK would be very likely to input into policy as a “best friend” and implement the EU’s decisions through UK legislation.

As a result, current UK rules in areas such as employment, consumer protection, competition law, financial services, life sciences regulation and

environmental policy would remain substantively unchanged. EEA members comply with freedom of movement of people, meaning it would be difficult for the UK to secure a qualification to this without a change of view on the part of other Member States.

The UK would no longer benefit from trade agreements between the EU and non-EU Member States. The UK could set its own import/export tariffs and negotiate its own trade deals with non-EEA member states (through EFTA if applicable) but could need to apply new “rules of origin” requirements to demonstrate the underlying source of products if those products are to avoid EU tariffs.

Like other EEA members, the UK would make a financial contribution to the Single Market but would be excluded from the costs and the benefits of EU membership in other respects.

Formal requirements

The UK’s membership of the EEA would require the agreement of all EEA members (i.e. the other 27 EU Member States plus Norway, Iceland and Liechtenstein).

As the EEA is an established framework, a UK transfer to the EEA rather than EU status could potentially be executed relatively quickly, so minimizing the period of uncertainty as to future arrangements.

Implications for business

This model would provide business with continuity in most key areas. Whilst changes to the legal structure would likely result in some increased complexity, this would be limited. However, the loss of the UK’s direct voice in EU decision-making could make it more difficult for business to press an “Anglo-Saxon” approach to regulation in EU policy development.

The EEA

The European Economic Area extends the EU Single Market to Norway, Iceland and Liechtenstein. EEA members benefit from, and are bound by, the EU’s Single Market rules covering free movement of goods, services, people and capital. They do not participate in the EU’s decision making structures or some other areas of EU competence.

EFTA

The European Free Trade Association consists of Norway, Iceland, Liechtenstein (members of the EEA and the Single Market) and Switzerland. EFTA concludes Free Trade Agreements with the rest of the world on behalf of its four members.

EEA Model: Summary

No tariffs	No change
Common standards	No change
Regulatory passport	No change
Trade agreements	Change: Via EFTA
Movement of people	Some restrictions?
Influence	Outside formal structures
Law	Indirect not direct
Contribution	Reduction

Alternative 3: Free trade agreement model

Background

A number of countries² currently have free trade agreements with the EU. Those countries are not part of the Single Market or the EU's other structures. Their agreements with the EU mean the reduction or removal of tariffs, and barriers to trade between them and EU Member States are minimized.

Historically, free trade agreements have focused on goods. The inclusion of services has been one reason for the complexity and duration of recent negotiations with Canada. This may be a relevant factor to consider, given the importance of services to the UK economy.

In practice, a free trade agreement with the EU will require that goods and services sold into the Single Market comply with EU rules. A free trade agreement is likely to include some liberalization with respect to services although this may well fall short of full Single Market access. Moving to a free trade agreement would significantly extend the UK's ability to set its own rules including in the area of immigration.

Key features

The terms of a new UK/EU free trade agreement would be specifically negotiated – a process which might be expected to take a number of years³. Based on experience of other agreements we can provide some insight into what it would, and would not, cover.

The UK and EU would likely commit not to apply tariffs and non-tariff barriers to a wide range of goods and services traded between them. Given the limited liberalization of services in free trade agreements, it is difficult to anticipate the depth with which a new agreement would cover services.

The UK would fall outside trade agreements between the EU and non-EU countries.

The UK would not formally fall within the scope of EU laws or benefit from “regulatory passporting”. In practice, it is likely that in some areas reflected in a new free trade agreement the UK would remain closely aligned to the EU approach and UK laws and standards would therefore follow those in the EU.

The UK would also be optimistic of achieving “third country equivalence” status for certain regulatory purposes leading to a degree of mutual regulatory recognition which might, to some degree, reduce the impact of the loss of full “passporting” or result in a redefined form of regulatory passporting in which similar outcomes are achieved by a slightly different mechanism.

The UK would set its own immigration policy and would not make a financial contribution to the EU.

² Excluding the EEA countries and Switzerland the EU has Free Trade Agreements fully in force with many countries ranging from Jersey and the Isle of Man to South Africa and South Korea. Other agreements (including with the USA and Japan) are in negotiation.

³ Under Article 50 – the formal process contemplates this negotiation starting only after the UK has agreed its withdrawal terms, although in practice negotiations on exit and the new relationship may well happen simultaneously.

Formal requirements

A new UK/EU Free Trade Agreement would need to be agreed between the UK and the EU and would then need to be ratified by all 27 remaining Member States. The UK would also need to agree new free trade deals with other countries to replace those from which it currently benefits via EU membership.

A UK/EU free trade agreement would be largely new and so, together with new third country free trade agreements, would likely take a significant period of time to finalize, so potentially increasing uncertainty.

Implications for business

Although the details are uncertain, this model could lead to an extended period of uncertainty and would be likely to result in some immediate significant changes. In particular, it is probable that there would be some (probably significant) reduction in “regulatory passporting” benefits currently enjoyed across some sectors. Controls on free movement of people would also be likely which could potentially have impacts particularly outside specialized or senior management roles.

Some of the core benefits of tariff-free trade and common principles applied in many areas may well survive, at least in some form and to some degree. In the longer term, the loss of the UK’s direct voice in EU decision-making could make it more difficult for business to press an “Anglo-Saxon” approach to regulation in EU policy development.

Free trade agreement model: Summary

No tariffs	Little change
Common standards	Reduced over time
Regulatory passport	Redefined or reduced
Trade agreements	Direct by UK
Movement of people	Set by UK (for UK) and EU (for EU)
Influence	Little specific influence
Law	Indirect some areas?
Contribution	None

Alternative 4: Full Divorce model

Background

It is possible that the UK will not wish, or will be unable, to agree any new relationship with the EU and will, eventually, leave the EU. In these circumstances, the UK's trading relationship with the EU (and other countries with which the UK has no special trading agreements) would fall back on the structure and the default arrangements provided under the rules of the World Trade Organisation ("WTO").

WTO

WTO is an international organization of 162 member countries.

Its main aim is to agree rules governing the conduct of international trade while reducing obstacles to trade (for example by setting limits on the maximum tariffs that countries can apply to trade in goods). However, the WTO has no provisions for free movement of labor. It also provides forum for negotiating trade agreements and a dispute resolution process to monitor and enforce participants' adherence to WTO agreements.

The UK is a member of the WTO, not only through its membership of the EU, but also in its own right. If the UK leaves the EU the UK will continue to be a member of the WTO. Current understanding is that the UK will have to confirm to the WTO that it will maintain the EU tariffs in the short term, but that these may change over time.

Key features

The UK would not automatically be entitled to tariff-free trade with the EU or any non-EU country. This would need to be negotiated on a case by case basis. By definition, in this model the UK would have no free trade agreement with the EU so tariffs would be imposed on UK/EU trade.

There would be no requirement for UK laws or standards to align with those applicable in the EU (although the UK's exports to the EU would need to continue to comply with EU rules). Whilst initially there may be limited change, UK and EU rules would diverge over time.

It is also possible that the principle of "equivalence" might apply in respect of some regulatory activity (as it currently does between the EU and US) but it is unlikely this would go far enough to prevent the loss of current "regulatory passporting". In the absence of a free trade agreement it is also likely that the administrative burden of trade, such as paperwork and border inspections, would increase significantly.

If the UK wished to preserve the benefits of current EU free trade agreements with third countries, it would need to negotiate new agreements. In the absence of new agreements, any benefits of tariff or non-tariff barrier free trade with those non-EU countries would be lost.

The UK would set its own immigration policy and would not make a financial contribution to the EU.

Formal requirements

This model would not require the UK to agree any new arrangements – only formal exit from the EU. As such this model could be implemented simply by the UK serving 2 years’ notice to leave the EU and agreeing withdrawal arrangements.

Implications for business

This model would result in the most radical change with the likelihood of new tariff and non-tariff barriers applying to the UK’s relationship with the EU and with other countries with which the EU has existing free trade agreements. The UK would not be formally aligned with the EU in any way making it likely that UK and EU markets and regulation etc. would diverge over time.

Whilst the loss of the UK’s voice in EU decision-making could make it more difficult for business to press an “Anglo-Saxon” approach to regulation in EU policy development, the UK would be free to work with business to create a wholly distinct regulatory environment, as well as to negotiate its own free trade agreements with third countries.

Full divorce model: Summary

No tariffs	Probable tariffs between UK and EU
Common standards	Reduced over time
Regulatory passport	Eliminated or radically reduced
Trade agreements	Direct by UK
Movement of people	Set by UK (for UK) and EU (for EU)
Influence	No influence
Law	Separated
Contribution	None

Overview of alternative models and possible outcomes

This table summarizes the basic models described above. In practice, the outcome of the process may well reflect an issue-by-issue solution.

	New terms	EEA	Free trade agreement	Full divorce
No tariffs	No change	No change	Little change	Probable tariffs between UK and EU
Common standards	No change	No change	Reduced over time	Reduced over time
Regulatory passport	No change	No change	Redefined or reduced	Eliminated or radically reduced
Trade agreements	No change	Change: Via EFTA	Direct by UK	Direct by UK
Movement of people	Additional restrictions?	Some restrictions?	Set by UK (for UK) and EU (for EU)	Set by UK (for UK) and EU (for EU)
Influence	No change	Outside formal structures	Little specific influence	No influence
Law	No change	Indirect not direct	Indirect some areas?	Separated
Financial contribution	Possible reduction	Reduction	None	None

Potential variations

Although the principle of these alternatives can be relatively simply stated, in reality the UK's relationships with the EU and other countries is highly complex. In assessing possible outcomes, and strategies to address the process, it is important for business to consider four particular questions:

- How will free movement of people be balanced against Single Market access? UK control of its own policy on immigration of EU nationals has been a core political theme of the referendum but there was no consensus within the “Leave” on the form or extent of controls or on the desirability and importance of the UK maintaining access to the Single Market. There also appear to be some differences of view between governments of various other Member States as to whether change in the application of the freedom of movement principle is desirable or appropriate.

If the UK is to continue to have full access to the Single Market (as envisaged in the New Terms and EEA models), the UK Government would need to accept that free movement of people would remain unchanged or the other Member States would need to accept some new restrictions on this principle.

This question has, to date, proved insurmountable in seeking to finalize Switzerland's EEA status. Unless the remaining Member States are willing to compromise or there is a further significant political change in the UK, this issue is likely to drive the UK's future relationship with the EU toward the Free Trade Agreement or Full Divorce models, which would represent the most radical change to the status quo.

- Will principles be applied consistently or variably? It is not necessarily the case that a single principle will be applied consistently across all activities. It is possible that the UK and EU could agree special treatment in some areas (e.g. mutual recognition of regulation of life sciences or financial services) without the UK remaining a full member of the Single Market. Indeed, the very preliminary implications from the UK Government's provisional working team are that the approach to the exit negotiations will likely be one which starts by taking a “pick and mix” issue by issue approach. In this context, businesses should consider how best to promote the issues most important to them as priorities in this process.

- Will there be change within the EU? The UK's referendum result has increased the level of debate within the EU as to the EU's future creating the possibility of change, either as part of a strategy to keep the UK within the Union or to reform a 27 member EU. Many of these initiatives are being examined by governments or politicians from individual Member States rather than the EU institutions themselves. Businesses should consider whether it would be appropriate to support these reform initiatives in individual Member States as well as at an EU level.
- How quickly will the process move? Any process to separate the UK from the EU will be complex as it will involve the unwinding of existing institutional, financial and legal arrangements large and small. However, finalizing agreement on new arrangements which involve significant difference from those currently in place will require agreement almost certainly from the UK, EU and all member states. If the UK Government seeks a fundamentally new arrangement this is likely to be a prolonged process taking a period of several years. Business should consider whether there are some areas in which clarity can be secured at an early stage of the process to mitigate the risks of uncertainty.

Appendix iii

Brexit – what now? Uncoupling UK law from the EU

Much UK law is currently linked to that of the EU. Ending the UK's membership of the EU will require significant uncoupling of the two legal systems.

This paper provides an introduction to the inter-relationship of UK law and EU law and the legal mechanisms that might be used to separate them. As the issues surrounding implementation are highly complex, this introductory paper tries to provide a clear outline that can act as the foundation for more detailed analysis.

UK Membership – legal status

UK law has historically taken the view that an international treaty (or non-UK law ratified by the UK Government) does not form part of the domestic laws of the UK unless and until it is given effect by, or pursuant to, an Act of the UK Parliament. In limited circumstances, the UK Government can give effect to treaty obligations without specific legislation. The EU law perspective is that the obligations of EU law apply throughout the EU as an automatic consequence of membership of the EU. This means that EU law will, on its own terms, no longer apply in the UK immediately after the UK stops being an EU Member State. As a result, the UK's membership of the EU operates on three levels:

- **International level:** For so long as the UK is part of the EU, the UK's compliance with the EU Treaties is governed by EU law. After the UK has left, it may still have obligations arising from international law. As a general principle, international law regulates relationships between states rather than the rights and obligations of citizens or business although there are significant exceptions, such as the EEA Agreement and fundamental rights provisions;
- **EU level:** As a result of EU membership, the relationship of an EU Member State with the institutions of the EU, and the Member State's compliance with its obligations under the EU Treaties¹, is regulated by EU law, as distinct from international and domestic law; and

- **Domestic level:** In UK law, the ECA² provides the UK law basis for the relationship between EU and UK law and gives EU law precedence over UK law. To implement Brexit the UK will need to amend or repeal the ECA and other legislation.

Categories of EU Law

EU law can be defined in the following principal categories:

- **EU Treaties:** The primary law of the EU. Binding on the UK as an EU Member State. The EU Treaties also contain important provisions that create rights and obligations for private persons throughout the EU, and which are directly enforceable in the UK for so long as it is part of the EU;
- **EU Regulations:** EU Regulations are binding and directly applicable and so do not require transposition by the UK into domestic law to be directly enforceable in the UK courts;
- **EU Directives:** Directives are binding upon Member States as to the result to be achieved but, with limited exceptions, are not directly applicable or enforceable in domestic law without Member States taking steps to transpose them. Directives are generally transposed into UK law by domestic primary or secondary legislation; and
- **Decisions of the institutions of the EU:** Some decisions of EU institutions are binding on the parties to whom they address, and tend to address matters specific to those parties and so can be relied on in the UK courts.

¹ The Treaty on the European Union (TEU) and the Treaty on the Functioning of the European Union (TFEU), referred to together as the "EU Treaties".

² The "ECA": The European Communities Act 1972 – the key UK statute implementing the UK's membership of the EU

Implementation of EU Law in the UK

The different categories of EU law described in this paper are implemented in UK law in different ways:

- Under EU law, some elements (including EU Regulations and certain provisions of the EU Treaties) are directly applicable, or have direct effect, in Member State domestic law. Section 2(1) ECA incorporates this category of EU law into UK law so that it takes effect in UK domestic law automatically without the need for further UK legislation. This mechanism provides a “short cut” to implement a wide range of EU legislation into UK law;
- Section 2(2) ECA provides a mechanism to give UK legal effect to EU law provisions that are not directly applicable and do not have direct effect. It gives power to the UK Government³ to make secondary legislation, such as statutory instruments, to implement any EU law obligation, without the need for further primary legislation. A large number of EU law provisions are currently incorporated into UK law through secondary legislation under this section. This secondary legislation can even amend primary legislation (section 2(4) ECA);
- Some other EU law measures which do not have direct effect are incorporated into the UK by other specific primary or secondary legislation. In some cases, this goes further than the relevant EU law and/or predates the EU law; and
- Section 3(1) ECA requires UK national courts to construe all primary legislation in line with EU law, as interpreted by the Court of Justice of the European Union (“CJEU”), and disapply any legislation that is inconsistent⁴. The effect is that rulings of the CJEU on the correct interpretation of EU law are binding in the UK.

As EU law takes effect in different ways, a variety of approaches would be needed to give effect to Brexit.

How might the UK implement Brexit in UK law?

The only formal process for the UK to leave the EU is that set out in Article 50 of the EU Treaty. This provides that, on exit, the EU Treaties will “cease to apply” to the UK. Whilst it is possible the UK’s exit could be executed by agreement (i.e. without triggering Article 50), we assume for the purposes of this paper that in any event the EU Treaties will no longer apply to the UK on Brexit.

Applying this assumption and by way of illustration, we outline in this paper three theoretical approaches (plus a variation of Option 2) that could apply to UK law on exit. These models are useful in understanding the key issues but, in practice, as we describe at the end of this paper, the actual process of withdrawal is likely to be far more complex.

Key points

Principal ways in which UK law incorporates EU law:

- Directly applicable or effective provisions of EU law are automatically recognized and enforceable in UK law under section 2(1) ECA;
- Provisions of EU law that are not directly applicable or effective are transposed into UK law by domestic primary or secondary implementing legislation. Much of this is done through secondary legislation enacted under section 2(2) ECA; and
- EU Court decisions on the interpretation of EU law are binding in the UK.

In some areas, the current UK regulatory regime relies entirely on directly applicable EU law provisions.

In other areas, the UK regime may incorporate EU law as part of the domestic framework. Sometimes UK law goes further than the minimum standards required under EU law.

³ As result of devolution, the Scottish, Welsh and Northern Irish devolved administrations have concurrent responsibility to comply with, transpose and implement the UK’s obligations to implement EU law which relates to devolved matters.

⁴ Where the correct interpretation of a provision of EU law is disputed, the national courts can refer the question to the CJEU under the Article 267 TFEU.

Option 1: Brexit with no domestic UK legal implementation

In this scenario:

- At the point at which the UK stops being a member of the EU no changes would be made to UK domestic legislation; and
- The ECA would remain in force in its current form, as would all other primary and secondary legislation giving effect to EU law.

It is relevant in this context that the implementation of specific legislation to repeal implementation of EU law would, in most cases, require an active decision of the UK Parliament. This is a matter that is subject to some political uncertainty so, to the extent there were no such active decision, there would be no domestic UK legal implementation of Brexit.

Section 2(1) ECA operates by giving force in UK law to any “enforceable EU right” within the meaning of that section. When the UK stops being an EU Member State directly applicable EU law rights will no longer be “enforceable EU rights” for this purpose. As a result, EU Regulations and directly applicable EU Treaty provisions will no longer have effect as a matter of UK domestic law⁵.

By contrast, all secondary legislation adopted under section 2(2) ECA and all other primary and secondary legislation giving effect to EU law would remain in force and would be unaffected by Brexit. As a result, EU legislation that is not directly effective in the UK would continue to apply as a part of UK domestic law unless and until the UK Parliament actively repealed or amended those laws.

However, although statutory instruments giving effect to EU law under section 2(2) ECA would not be rendered automatically invalid, their provisions would no longer serve the purpose for which they were enacted, namely to give effect to the relevant provisions of EU law. There is a risk that this could open up those provisions to challenge in the UK national courts.

In addition, although the provisions of indirectly effective EU law (primarily EU Directives) would continue to apply through UK implementing legislation, they would arguably be “frozen” in that form and would not track any changes to the underlying EU law unless and until amended to that effect by the UK Parliament.

In some areas, for example the telecommunications sector, UK regulation is constituted by a combination of directly applicable EU Regulations and domestic law which “fills in the gaps”. This scenario would be particularly unsatisfactory for the affected areas as parts of the regime would remain whilst others would no longer apply.

Option 2: Remove EU-influenced law from UK law

In this scenario the UK Parliament would pass legislation to repeal the ECA in its entirety and without replacement.

In a variant to this option, (Option 2A in the table of options), Parliament could go even further and legislate to repeal all UK primary and secondary legislation which implements EU law in the UK, with effect from the date on which the UK leaves the EU.

This would represent an active decision by the UK Parliament to “turn the UK’s back” on everything connected with the EU.

Repealing the ECA without replacement would have the following results:

- All directly applicable and directly effective provisions of EU law (including all EU Regulations), which have no domestic implementing legislation, would immediately no longer apply; and
- All secondary legislation adopted under section 2(2) ECA to implement other provisions of EU law would lapse as at the date that the repeal took effect, unless such provisions were expressly saved by the repealing legislation.

⁵ There is a separate question about whether rights acquired under the EU law before Brexit could be enforced after Brexit in these circumstances, which we consider below.

If the legislation were more wide-ranging it might try to terminate the effect of all UK primary or secondary legislation which implements EU law. However, in practice it would be challenging to identify precisely the UK law falling into this category as some UK laws reflect the same principles as are embodied in EU law, whilst not being explicitly derived from those EU laws.

Under section 16 of the Interpretation Act 1978, unless the repealing legislation expressly provides otherwise, the repeal would not affect the previous operation of the enactments repealed or lapsed. Rights acquired, obligations accrued or liabilities or penalties incurred under an EU-derived UK law before the date of repeal would not be affected. For example, a person who became liable to a penalty as a result of contravening, before the date of Brexit, a requirement imposed by a provision of an EU Regulation would still be liable to pay the penalty for that breach.

In this scenario large areas of regulation that are regarded as non-controversial and which have been implemented throughout the EU would no longer have effect, leaving considerable gaps in the legislative and regulatory framework in the UK.

Option 3: Retain all EU law as part of UK law

In this scenario the UK Parliament would enact new legislation with the intention of preserving the application of EU law as part of UK law following Brexit. The mechanism used could be amendment of the ECA or the introduction of a new “Brexit Act”.

This option might be favored if, for example, the UK wishes to preserve the domestic law status quo to provide stability at the point of Brexit, with a view to Parliament making changes progressively following Brexit⁶.

An amended ECA or a Brexit Act could ensure the preservation of secondary legislation enacted under section 2(2) ECA. Indeed, a Private Member’s Bill introduced in the UK Parliament in 2013, but not enacted, sought to repeal the ECA whilst providing that all secondary legislation previously enacted under it would continue in force until subsequently amended or repealed. Other primary and secondary legislation implementing EU law would remain in place, as under Option 1.

The position of EU law that is currently directly applicable or effective in the UK (EU Regulations and Treaty provisions) would be more complex.

In theory a revised ECA or a Brexit Act could give these rules a new legal basis in UK law – most likely as new secondary legislation.

However, the construction and operation in a non-EU state of provisions which started life as EU legal instruments would not be straightforward. To take one simple example, it is not clear how an EU Regulation providing for the involvement of an EU institution or and/or EU level procedures would operate in this scenario.

Given this, in practice it is likely that every specific provision of EU law will need to be reviewed before the date of Brexit. To the extent that the UK Parliament wishes the effect of those provisions to continue, even on a temporary basis pending more substantive reform, technical amendments will need to be considered to ensure the status quo is preserved.

⁶ One possibility is that a Brexit Act could be constructed to include a “sunset clause” so legislation would fall away automatically after an extended period allowed to preserve an amended regulatory regime.

Summary

	Option 1 No domestic UK legal implementation	Option 2 ECA repealed; no replacement	Option 2A*** All UK implementation of EU law repealed	Option 3 Retain EU law in the UK
EU Treaties (directly applicable or effective provisions)	No continuing impact in UK law	No continuing impact in UK law	No continuing impact in UK law	Continue to apply in UK law**
EU Regulations	No continuing impact in UK law	No continuing impact in UK law	No continuing impact in UK law	Continue to apply in UK law**
EU Directives (As implemented by secondary legislation under section 2(2) ECA)	Continue to apply in UK law*	No continuing impact in UK law	No continuing impact in UK law	Continue to apply in UK law**
EU Directives (As implemented by primary or secondary legislation other than section 2(2) ECA)	Continue to apply in UK law**	Continue to apply in UK law**	No continuing impact in UK law	Continue to apply in UK law**

* Directives implemented via section 2(2) ECA potentially challengeable in the national courts

** In some cases operation is likely to be unclear unless specific amendments made

*** This Option is a variation of Option 2

Some potential practical complexities

In this section, we consider some of the issues that will need to be borne in mind when assessing the practical implementation of Brexit in UK law.

1. Identifying relevant EU Law

As will be clear from the summary section, it is unlikely that any of the three options described will be implemented in their purest form.

The primary reason for this is that it is unlikely to be considered either practical, or desirable, to abandon immediately all UK law that reflects EU law, as significant elements are likely to be considered appropriate to be retained as UK law in any circumstances. Similarly, if the UK leaves the EU it is unlikely to be politically acceptable to retain all EU law as part of UK law.

So a key issue will be to determine which elements of EU law are to be retained within UK law following Brexit, whether on a permanent basis or “provisional” basis pending longer term amendment.

2. Need for a smooth transition

As already discussed, there is a significant risk that the Brexit process could create significant gaps in the UK’s legal and regulatory structure and/or uncertainty as to its effect.

If, for example, post-Brexit all EU law that takes effect through section 2(1) ECA no longer has effect but all EU law that is transposed into UK law by domestic primary legislation or secondary legislation remains in force, the resultant UK regime would in some areas be a patchwork of incomplete and inconsistent elements which would be difficult to operate.

Whatever political decisions are eventually made regarding the nature of the future relationship between the UK and EU, on a practical level it will be important to ensure the process provides for a coherent process of transition.

3. Changing EU Law

The uncoupling process will have to be done in a way that allows an effective transition, and does not undermine the UK’s domestic regulatory and legislative coherence.

Understanding the complex task ahead is key to effectively analyzing the implications of Brexit and engaging successfully now with the EU and

the UK Government. There is a risk that if the UK Government implements Brexit in a way that does not achieve regulatory and legislative coherence, then this could lead to uncertainty and legal anomalies in policy areas and industry sectors in which EU law forms an integral part. The UK Government has already begun the task of mapping how EU law interacts with and/or affects all aspects of UK law. Businesses should now be doing the same in respect of their business so as to identify the potential risks and opportunities in the transitional period.

4. CJEU judgments

The CJEU makes definitive interpretations of EU law. National courts of EU Member States refer to the matters of interpretation to the CJEU (the national courts determine how EU law, as interpreted by the CJEU, applies to the facts of a specific case). A number of issues could arise, including:

- It is likely that, following Brexit, the UK will retain laws that currently implement EU law in the UK, for example, some of the primary or secondary legislation that currently implements EU Directives;
- The UK courts may well continue to treat relevant CJEU judgments which have already been applied by the UK courts before Brexit as having some precedential status in interpreting those laws. However, it is possible those decisions might be open to challenge in the UK courts once the UK has left the EU;
- It is less clear whether pre-Brexit decisions of the CJEU which have not yet been applied by the UK courts (e.g. decisions taken by the CJEU on a reference from the courts of another EU Member State) would be treated as binding precedent; and
- It is also unclear what, if any, precedential weight would be given to post-Brexit decisions of the CJEU regarding relevant EU laws. It might, for example, be given similar status to that which the UK currently gives to decisions of other Common Law jurisdictions (e.g. Australia).

5. Mutual recognition

There is a substantial issue relating to whether actions taken by individuals and businesses after Brexit pursuant to UK laws that originally implemented EU law rules would continue to have effects under the EU regime in the remaining EU Member States.

One practical example might be the Extradition Act 2003, which provides a domestic basis for the European Arrest Warrant (“EAW”). Unless amended, the Extradition Act 2003, as primary legislation, would continue in force post-Brexit and provide a continuing legal basis for the EAW regime as a matter of UK law post-Brexit.

However, requests from the UK under the EAW regime would only continue to be acted upon by other EU Member States following Brexit if, presumably as part of the agreed future relationship, those states and/or the EU introduce laws to that effect.

6. Devolution

The Devolution Acts currently constrain the flexibility for the devolved administrations of Scotland, Wales and Northern Ireland by requiring them not to legislate or act contrary to EU law, and gives those administrations concurrent responsibility to comply with, transpose and implement the UK’s obligations to implement EU Directives where they relate to devolved matters.

After Brexit, assuming the Devolution settlement remains broadly as it is presently, it would be for the devolved administrations to decide whether to retain, repeal or amend provisions of EU law in relation to devolved matters. As part of the Brexit settlement, a decision will need to be made whether this freedom would continue to be constrained in any way.

The Devolution Acts

The Scotland Act 1998, the Government of Wales Act 2006 and the Northern Ireland Act 1998 (together, the “Devolution Acts”) are the legislation that gives effect to devolution to nations of the UK.

There is a strong possibility that the Devolution Acts will need to be amended by the UK Parliament to take account of Brexit. There is a political convention that the UK Parliament will not normally legislate with regard to devolved matters without the consent of the Scottish Parliament. Therefore, there is a significant possibility that there will be substantial political pressure on the UK Parliament to obtain some form of consent from, at least, the Scottish Parliament to make changes to the ECA.

7. Regulatory bodies

Brexit will potentially lead to the need for new domestic regulatory authorities in areas where oversight was previously carried out at an EU level.



What should businesses be doing?

The scale of the task of reviewing the entire legislative and regulatory framework of EU law in the UK in advance of Brexit taking effect is considerable – even if the UK simply wishes to ensure the status quo prevails from a pre-Brexit to post-Brexit settlement, rather than conduct an immediate overhaul of EU law in the UK before Brexit. The uncoupling of the EU and UK legal systems is therefore likely to dominate the domestic policy and regulatory agenda for the foreseeable future.

The domestic Brexit process represents a risk of uncertainty and instability for businesses operating in a range of industry sectors in the UK, but for businesses that equip themselves effectively it also can be an opportunity. Businesses are well placed to analyze which provisions of EU law matter to their business and what is needed in order to ensure that the transitional period is not unduly disruptive to their operations.

Businesses need to start now reviewing the impact of EU laws on their operations and preparing to engage with the UK Government and EU Institutions during the transitional phase about the desired terms of the UK's withdrawal negotiations, and to support Government through the transition.

Questions to ask might include:

- Is access to the Single Market of paramount importance for your business?
- Are your operations particularly at risk if there is a less-than-smooth transition to a post-Brexit settlement in the UK?
- How can the UK Government best repatriate EU regulatory regimes and what, if any, improvements could be made in the repatriation process?

Business should immediately engage with the EU and the UK Government to make clear their priorities in the process, whilst also assessing the potential impact of the various possible outcomes for their business operations.



Appendix iv

Brexit clauses

What is a Brexit clause?

A “Brexit clause” is a contractual provision which triggers some change in rights/obligations as a result of a defined Brexit-related event. The clause therefore sets out two basic things: (a) the specific Brexit related event triggering the clause; and (b) the contractual consequences of that event.

Are Brexit clauses fundamentally different from other “change” clauses (including Material Adverse Change (“MAC”) clauses)?

No.

Many agreements include provisions addressing the potential impacts of future change, ranging from broadly based MAC clauses to very specific provisions for the impact of change in a particular law or regulation or in the price of a particular commodity. Brexit clauses are just a variation on this familiar theme.

Why use a Brexit clause?

A Brexit clause can provide protection against adverse circumstances arising in connection with Brexit. However, as with any “change” clause, there are challenges. Can the parties define and agree a trigger event which is sufficiently specific to be contractually enforceable? Is it realistic to predetermine the consequences of a future event? What should the consequences be if the event occurs? By their very nature, change clauses can be vulnerable to the parties interpreting them in different ways.

Is “Brexit” an appropriate trigger for change?

Technically, “Brexit” would occur when the UK formally stops being a member of the EU. However, it is currently very unclear what the post-Brexit trading landscape will look like and how Brexit would, in practice, take effect, which makes it more difficult to anticipate precisely what effect Brexit will have on business agreements.

At its most extreme, Brexit could result in all UK laws which have derived from the EU being repealed and barriers to trade and movement of goods, services, people and intangibles being erected between the UK and EU. Equally, it is possible that the UK eventually decides not to trigger Article 50, and remains in the EU, but secures agreement to significant changes. However, both these outcomes currently appear unlikely.

Even if the UK eventually formally stops being a member of the EU, it is probable that many of the UK’s laws and many aspects of the trading position between the UK and EU will remain unchanged, e.g. because UK law needs to remain aligned with EU law to facilitate trade or because the UK law in question is not derived from EU law. It is also likely that Brexit changes will take effect over a period of time rather than on a single day.

Given these uncertainties, it will be difficult for parties to a contract to agree an effective clause which triggers change just by using the simple phrase “if Brexit occurs” as “Brexit” may, in practice, mean different things. It is more likely to be appropriate, and more likely to create an effective clause, to define a specific trigger(s) which is relevant to the contract.

Could Brexit trigger a MAC, change or force majeure clause?

It is unlikely that, in most cases, the result of the referendum would itself trigger an existing, broadly drafted, clause that is triggered on a “material change” or similar language. However, it is possible that the consequences of the referendum (for example, changes in exchange rates or deterioration in the economic prospects of a business) could satisfy the thresholds or fall within the scope of some existing clauses with specifically defined MAC triggers (some of which may have been developed with Brexit in mind, e.g. in finance documentation) but this will only be the case in specific circumstances.

It is more likely that some specific aspect of the Brexit process, such as regulatory change or imposition of tariffs could trigger a generic clause. For example, if a UK entity is no longer capable of being authorised to provide certain services within the EU this could constitute a “material adverse change” or even “force majeure”.

It will be important to review existing significant agreements to assess the potential impact of various Brexit related events on MAC, change and force majeure clauses and to have Brexit in mind when negotiating future clauses.

What types of trigger might a Brexit clause include?

When assessing the nature of a Brexit clause it is important to consider the specific context of the agreement. For example, both the appropriate trigger and the consequences of a clause are likely to differ between an agreement with a relatively short horizon (e.g. a share purchase agreement or capital markets underwriting agreement) and a long term agreement (e.g. a joint venture or strategic commercial supply contract).

The following are some categories of potential triggers for a Brexit clause:

- A specific change in the law or the imposition by government of specific costs (Example: “*A change in the laws applicable to [relevant activity] such that [Party A] is no longer entitled by law to sell [product or service] in the member states of the European Union.*”)
- A divergence between the rules applicable in the UK and those applicable in the EU (Example: “*The laws applicable to [relevant activity] in the United Kingdom ceasing to be [substantially similar] to those applicable to [that activity] in the European Union*”)
- A loss of “passporting” benefits currently available under EU rules (Example: “*A change in the laws applicable to [relevant industry] such that [Party A] is no longer entitled by law to sell [product or service] in the member states of the European Union.*”)
- Tariffs or other specific costs being imposed (Example: “*Tariffs being imposed upon the sale, licensing or other transfer of [specified goods or services] from the United Kingdom to a member state of the European Union.*”).

In specific contexts it may also be appropriate to consider clauses linked to political events (such as the service of a notice under Article 50 or calling of a UK General Election) or market events (such as exchange rate movements through particular thresholds).

A simple clause providing a trigger “when the UK ceases to be a member of the European Union” may itself create uncertainty and is unlikely to be desirable in most cases. If, for example, as part of agreed transitional arrangements some elements of EU structure and laws continue to apply to the UK for a transitional period after “exit”, such a clause may not operate as originally intended.

What potential consequences might a Brexit clause provide for?

The following are some categories of consequences which might be provided for in a Brexit clause:

- A right for one, or either, party to terminate the contract. In this case it will be important to be clear whether the associated consequences of termination and/or termination mechanisms treat this as a “fault” or “no-fault” termination
- A process of negotiations between the parties with a view to agreeing the consequences of the relevant trigger. In this case it will be important to be clear as to the consequences if no agreement is reached and the timeline/end-stop date for such negotiations
- A specific change in the effect of the contract (Example: *“If the United Kingdom ceases to be a member of the European Union, then with effect from the date of such event [the United Kingdom will not be part of the Territory][the Territory is amended to include the United Kingdom and the European Union]”*)
- Allocation of responsibility for addressing a particular consequence (Example: *“If there is any change in the law applicable to [relevant activity] in the United Kingdom, [Party A] will be responsible for ensuring compliance with such revised law”*)
- Allocation of responsibility for particular costs (Example: *“If tariffs are imposed upon the sale, licensing or other transfer of [specified goods or services] from the United Kingdom to a member state of the European Union, those tariffs will be paid by [Party A]”*)
- Some combination of factors (Example: *“If [Brexit related event] occurs, [Party B] will be responsible for [specific Brexit related action] PROVIDED THAT [Party A] will reimburse and pay to [Party B] all costs and expenses reasonably incurred in connection with such [specific Brexit related action] up to a maximum aggregate amount of £[]”*).



Appendix v

Brexit: trade associations and competition law

How to discuss your industry's reaction to Brexit without falling foul of competition law.

Given the economic, political and legal uncertainty following the “Leave” vote, businesses will understandably want to discuss with each other how Brexit will affect their industry and explore how they can help shape the future of the legal and regulatory landscape affecting it.

Such discussions will be valuable and necessary. However, communications between competitors attract suspicion from competition authorities, who will be concerned to ensure that those discussions do not breach competition law rules.

These guidelines, which apply to all formal and informal discussions, are intended to help businesses keep on the right side of competition law when entering into such discussions.

Legal framework

It is important to remember that agreements and other practices that prevent, restrict or distort competition are prohibited under both UK and EU competition law.

Although the UK's legal and trading landscape may be changing, businesses must remain compliant with competition law. Breaches can have serious consequences for companies, trade associations and the individuals involved, including large corporate fines, disqualification as a director, imprisonment and personal fines, reputational damage and damages claims.

Permitted discussions

Businesses can discuss the following issues, including in the context of Brexit discussions, but only to the extent that those discussions do not involve pricing or other competitively sensitive information:

- General market trends and publicly available information;
- Government or regulatory policy;

- Joint industry lobbying and promotion initiatives; and/or
- Other purely technical/non-commercial issues.

It is also possible to collect, share and disseminate certain information, provided that this relates to historical data and is appropriately aggregated and anonymized (discussed further in this note).

If meetings are specifically intended to discuss Brexit and develop a joint lobbying effort, the discussion should be limited to this topic. Only information which is necessary to develop a strategy and a related lobbying position should be disclosed.

Prohibited discussions

Some general guidelines on what topics must be avoided are set out in this note. However, the golden rule is that businesses should not share information which would reduce competitive uncertainty in the market, or could help inform a competitor's future commercial strategy.

No discussion of pricing information

Businesses should never discuss pricing practices or intentions. Competition authorities will be particularly concerned that discussions on Brexit should not, for example, provide businesses with the opportunity to insulate themselves from the current economic uncertainty by fixing prices. Businesses should not discuss or agree:

- Current prices (including information relating to discounts) or financial terms and conditions;
- Future pricing plans, including the timing of proposed price changes; and/or
- Past pricing levels, if that information allows inferences to be drawn about current or future pricing.

No discussion of other types of competitively sensitive information

Businesses should also not agree or discuss their own approach to any other matters that could be regarded as competitively sensitive. For example, businesses should never agree or discuss:

- Current or future marketing strategies, business, marketing or operational plans or strategies;
- Current or future profit margins or profitability targets;
- Customer lists or any other customer-specific information (including negotiating strategies and proposed contract terms);
- Cost information;
- Capacity or production, export, purchase and sales volumes; and/or
- Any other matter on which businesses compete.

Businesses should also not use Brexit related discussions to agree to take steps, for example, to protect the UK markets from competition from the rest of Europe.

Before, during and after meetings – procedural safeguards

In relation to any meetings or discussions, an agenda should be prepared in advance. At the beginning of each meeting, it should be made clear what discussions are permitted and what are prohibited. Official minutes should be prepared following each meeting, summarizing the discussions that took place.

If a discussion strays into prohibited matters, participants should leave the meeting immediately, and their departure (and the reason for their departure) should be noted in the official minutes. If the discussion is informal and/or no minutes were taken, legal advice should be sought immediately.

Industry publications and reports

As part of an industry lobbying effort, trade bodies may wish to prepare economic reports to support their position. This may require members to provide specific, potentially sensitive, information. If that is the case, a single, independent employee of the relevant trade body should be designated to collect the relevant information. That company-specific information should never be disseminated to members.

Instead, the information disseminated to members must be sufficiently historic to be no longer useful for taking business decisions (at least 12 months old – or longer depending on the business cycle in the industry concerned), and aggregated to prevent identification of information about individual members.

In addition, information should be disseminated to certain named individuals only, who are not sales or marketing staff or other “front-line” employees.

Appendix vi

Brexit and UK related M&A

What might the impact of the referendum result be?

The outcome of the UK's referendum on its membership of the European Union creates a number of near-term uncertainties.

In this paper, we discuss some of the immediate legal issues and questions which arise following the result in relation to M&A deals involving the UK.

The current state of play

It is important to remember that whilst the referendum result may provide a political mandate for a Brexit, its legal status is only advisory and not binding. In addition, it provides no guidance about the form which the UK's future relationship with the EU and the rest of the world should take. The formal process for a Brexit would also not start unless and until the UK delivers a notice under Article 50 of the Treaty on European Union. This would trigger a two year transitional period for withdrawal arrangements to be agreed, at the end of which (absent an agreed extension to the process) the UK would automatically leave the EU. The difficulties inherent in agreeing the withdrawal arrangements in this time frame has already generated intense political discussion about when the UK should issue its Article 50 notice. Until it does so, a Brexit is not inevitable.

Assuming that an Article 50 notice is issued, the potential legal forms that a Brexit might take is covered in Appendix ii. Possible models for the UK/EU relationship. There are a range of possible alternatives, ranging from full European Economic Area ("EEA") membership (likely accompanied by continued free movement of people and an EU-budget contribution) to the UK being unable to negotiate a trade agreement with the EU and falling back on its World Trade Organisation ("WTO") membership and WTO default rules. It is clear that depending upon the model chosen, the outcome and related issues will be different.

Impacts on UK-related M&A

Commercial

From a commercial perspective, the uncertainty flowing from the referendum result is likely to create both risks and opportunities for buyers and sellers of UK and European assets. For example, concerns around the uncertainty about the future ability of UK companies to sell goods or services into the EU may have a negative effect; conversely opportunities may arise in terms of pricing, including as a result of currency movements, or where companies decide to establish a base of further operations inside a revised EU. The effect of the result is also likely to vary significantly between both individual companies and industry sectors.

Legal

No laws have changed as a result of the referendum result and there is no certainty that any laws will change. Even following a Brexit, the laws governing M&A transactions in the UK are unlikely to change significantly in the short-term, because M&A is subject to limited amounts of EU derived law and regulation. However, we think it is possible, even at this early stage, to identify certain immediate issues:

1. Signed deals that have not yet completed: has a MAC occurred?

Parties to deals which signed before the referendum result but which have not yet completed may, if the terms of the deal include a termination right in the event of a material adverse change ("MAC"), wish to consider the extent to which a MAC has now occurred. This will depend entirely on the drafting of particular clauses, and many acquisition agreements will specifically have been drafted taking the referendum into account. However, where a company's business model is subject to particular negative effects as a result of the current outcome (perhaps, for example, where an acquisition target has had to issue a profit warning as a consequence of the referendum result), there may be reasonable

grounds for asserting that a MAC has occurred. This position should be considered on a deal-by-deal basis.

2. Future deals: Brexit conditionality

In addition to standard MAC clauses, it is likely that acquirers will wish in future to negotiate bespoke MAC and conditionality clauses in acquisition agreements to provide themselves with increased flexibility, given the various potential outcomes of the UK's exit negotiations. For example, depending on the industry sector concerned, conditions relating to future passporting rights, specific changes in law or regulation, or potential post-Brexit tariffs may start to appear.

3. Merger control: a potential for greater political interference in UK-related deals?

Currently, the EU merger control framework acts as a constraint upon political interference in merger control decisions. The European Commission reviews transactions solely on a competition-based test (whether or not the transaction will “significantly impede effective competition” in the EU) and there are limited exceptions where EU Member States can intervene to protect specified “legitimate interests”. With the loss of this system following a Brexit, it is possible that UK merger control could become more politicized or locally-focused. This could impact on deal clearance certainty and necessitate the use of political avenues to secure clearances.

And at a practical level, certain transactions will also no longer benefit within the EU from a “one-stop-shop” merger control review by the European Commission, and will instead require review by both the European Commission and the UK's Competition and Markets Authority. This may increase execution risk and extend deal timetables and costs.

4. Public M&A: the Code will continue

While it is correct from a technical perspective that the UK Takeover Code implements the EU Takeovers Directive, the Code existed in substantially its present form before the implementation of the Directive and has governed UK public takeovers for over 40 years. While small amendments may therefore be made to reflect a Brexit, it seems likely that the Code will continue in place in substantially the same form and will continue to be developed to ensure that the UK remains at the forefront of takeover regulation worldwide.

5. Private M&A: could cross-border mergers involving companies incorporated in the UK cease?

Private M&A is significantly less regulated in the UK than M&A relating to public companies. Accordingly, the potential for a Brexit to affect legal aspects of UK private M&A activity is even more limited. One potential impact of a Brexit, however, would be on the ability of UK-incorporated companies to make use of the EU cross-border merger regulations, which enable companies to merge with or into companies incorporated in other EEA states. Although the UK may be happy to continue to apply relevant legislation after a Brexit, it remains to be seen whether EEA states would agree to reciprocate. That said, cross-border mergers have remained only an occasional tool in the UK, so any decision by EEA states not to do so may have limited impact.

6. Due diligence and warranty packages

The range of potential outcomes from the UK's exit negotiations will also need to be considered by buyers during due diligence and in the context of the warranty and indemnity protections and undertakings built into acquisition agreements. The scope of Brexit-specific due diligence will develop as more information is known about how the referendum result might be implemented, but we expect that increasingly a target's readiness for a Brexit (of any type) in key business areas (e.g. geographic structure, staffing (profile and locations), contractual structure, IP arrangements and payment flows), together with its internal Brexit-planning, will be an area of interest. In particular, a Brexit of any type could affect a target's key contracts. Likely areas of contractual due diligence focus in a Brexit context will include change of control provisions, territorial scope and the potential effects of regulatory change.

7. Intellectual Property Rights

Following a Brexit, and absent any intervention by the UK government, all pan-EU intellectual property rights would cease to apply in the UK, although national IP rights would likely remain unaffected, at least in the short term. The UK government may choose to deal with this either by allowing all such EU IP rights granted up to the date of Brexit to continue to apply in the UK, or by instituting a form of conversion so that they could be converted into national rights. An alternative may be that businesses would have to re-apply for protection for their key IP as national rights. Buyers and sellers will need to take these potential outcomes into account as they structure deals to ensure that warranties and representations are not inadvertently breached or any necessary actions are taken to ensure IP rights are protected.

8. Business sales and employees: might TUPE requirements be relaxed?

At present, under the TUPE regulations, following an acquisition of assets constituting a business (as opposed to the shares in a particular company), acquirers have to employ existing staff of the transferor on their current terms and conditions. Even if the UK decides to retain the "automatic transfer" principle after a Brexit, it is likely that it would become easier to change terms and conditions of employment after a transfer. TUPE was reformed in 2006 and again in 2014 and it was recognized on both occasions in the UK that it would be helpful to allow more flexibility around post-transfer harmonization of terms and conditions, but that this was very difficult to achieve in light of existing European case law. This barrier to future reform could well be removed after a Brexit.

9. Restrictive Covenants

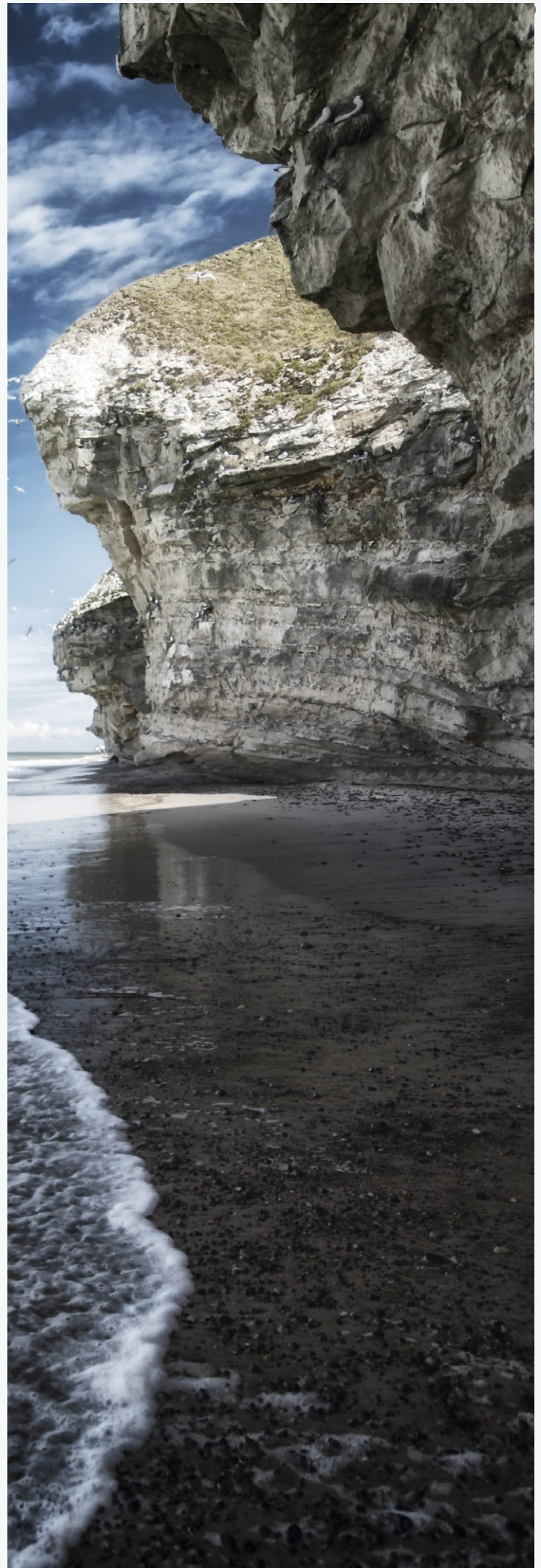
As more about what the outcome of the referendum result will be is known, it will be prudent to consider existing and proposed restrictive covenants in acquisition agreements and ensure that their drafting is still appropriate in the context of a Brexit. Drafting by reference, for instance, to the "European Union" or "European Economic Area" may not continue to produce the same outcomes following a Brexit.

10. Dispute provisions: will UK jurisdiction clauses and judgments be recognized and enforced?

The risk that a Brexit might lead to jurisdiction clauses in favor of a jurisdiction in the UK not being respected by courts in the remaining EU Member States, or that English judgments will not be easily enforced across the EU following a Brexit, is limited. This is because the EU is subject to the global jurisdiction and enforcement set out in the 2005 Hague Convention on Choice of Court Agreements. Like every EU Member State, except Denmark, the UK is currently subject to the 2005 Convention by virtue of its membership of the EU, but if and when the UK leaves the EU, it will very likely accede to the 2005 Convention as an independent contracting state. It can do that even without the cooperation of the EU.

The 2005 Convention guarantees that exclusive jurisdiction clauses in favor, for example, of English courts will continue to be respected in the EU in most civil or commercial disputes of an international nature, and that English judgments can be enforced there with relative ease, whatever the outcome of the negotiations with the EU.

A Brexit will also not affect the enforcement of London-seated arbitration awards, which will continue to be subject to the enforcement regime under the New York Convention, to which all EU Member States are a party.



Contacts

For more information, or advice on developing your practical response strategy contact your usual Hogan Lovells contact, a member of the Brexit team or email Brexit@hoganlovells.com

For more resources on readying your business for Brexit, and our latest thinking, visit our Brexit Hub at: www.hoganlovells.com/brexit



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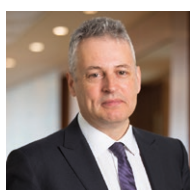
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