BREXIT BRIEFING

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OVERVIEW

What is it all about?

Ever since the United Kingdom's entry into the European Economic Community in 1973, Britons have been concerned about the gradual erosion of sovereignty and the widening powers of the European Commission. The demand for a new referendum on the UK's membership gained momentum in the 1990s following the painful negotiation of the Maastricht Treaty, which initiated a path towards a strong reinforcement of EU powers and the weakening of the unanimity rule in its decision making system.

In more recent years, the United Kingdom Independence Party (**UKIP**) have gained more and more traction in their demand for a referendum on membership. Following further gains by UKIP at the local-election level and enormous progress by UKIP at by-election level, the Conservatives decided to include the offer of an early referendum in their Manifesto for the 2015 General Election.

In accordance with the European Union Referendum Act 2015 (the "**Act**"), the question that is to appear on the ballot papers is :

> “Should the United Kingdom remain a member of the European Union or leave the European Union?”

The alternative answers to that question that are to appear on the ballot papers are:

> “Remain a member of the European Union” or
> “Leave the European Union”

In his letter of 10 November 2015 to Donald Tusk, the President of the European Council, Mr Cameron made four key demands. Those relate to:

- **Economic governance:** including acceptance of demands that the EU can have more than one currency, and that non-Eurozone taxpayers should never be financially liable to support the Eurozone as a currency.

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- **Competitiveness:** harmonising of many aspects of the single market, making the free flow of capital, goods and services across the market easier, and cutting regulation (a common Tory theme), all designed to boost competitiveness and productivity of the European Union and to drive growth and jobs.
- **Sovereignty:** including ending Britain's obligation to work towards a closer union and to enhance the role of national parliaments.
- **Immigration:** removal of the immediate entitlement to in-work benefits and social housing for migrant workers from the EU and some restrictions on the free movement of workers for future new EU members.

Of these four issues, it is the fourth - immigration - that is most specific and has been the focus of most media attention and upon which the Prime Minister has struggled to persuade his fellow heads of government to agree with him. The Prime Minister stated in his letter to Donald Tusk that if he can reach agreement with his counterparts on each of these four areas, he will campaign to keep Britain inside a reformed EU.

When could it happen?

This is the big question on which there has been a huge amount of speculation. Once the progress achieved in dealing with the four issues becomes clearer that will probably be the point at which the Prime Minister announces the date of the referendum. This announcement is expected at the end of February, or early March.

The Act provides that the referendum must be held no later than 31 December 2017. In addition, it must not be held on either 5 May 2016 or 4 May 2017, in order to avoid clashes with local and regional elections.[1]

Campaigning on the referendum could in theory however take place in twin track with the local and regional elections.

The most likely dates being discussed at the moment are June/July or September/October 2016. Much will depend on the outcome of the Prime Minister's negotiations with his fellow heads of government and his view as to whether a long campaign or a short campaign will better suit his objectives. In any event, before the beginning of the final 10-week period (that is, the period of 10 weeks ending with the date of the referendum), the Secretary of State must publish two reports. The first must contain: (1) a statement setting out what has been agreed with member states of the EU following the Prime Minister's negotiations; and (2) the opinion of the Government on what has been agreed.[2] The second must contain: (1) information about rights, and obligations, that arise under EU law as a result of the UK's membership of the EU; and (2) examples of countries that do not have membership of the EU but do have other arrangements with the EU (describing, in the case of each country given as an example, those arrangements).[3]

Would a vote to leave result in the UK immediately exiting the European Union?

No, the results of the referendum will be taken as a political mandate for the Government in one direction or another, but will have no effect on the actual UK membership of the EU. Thus, in the case of an OUT vote, there would be a period of transition for the UK to negotiate with its EU partners the actual terms of its exit from the EU.

How long would it take for the UK to actually leave the European Union in case of a vote to exit?

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The EU is based on international treaties, which have created a rather complex relationship between the UK and the EU as a whole, and — through the EU — between the UK and its members. This includes cross-legal as well as financial obligations that cannot be terminated via the unilateral decision of any EU member. The Lisbon Treaty introduced for the first time a basic procedure for "withdrawal from the Union". It fixes the requirement for the "withdrawing Member State" to officially notify its intention to the European Council. After that, a negotiation would need to start, somehow similar to an accession membership negotiation, but in "inverted terms", to clarify chapter by chapter and matter by matter the real effect of such decision, creating a tailor-made situation that can be acceptable for all parties. There is no comparable precedent for such an agreement, but if we compare with accession agreements, or with the negotiation of association agreements with third countries, it is difficult to imagine that it would take less than a year. This "Withdrawal Agreement" shall set out "the arrangements for [the State's] withdrawal, taking account of the framework for its future relationship with the Union". Thus, this will be a complex Treaty with details on very different topics such as security and defence, social matters, financial matters, trade and access to the internal market.

From the moment of the notification to the Council, the UK would not be allowed to participate nor vote in any European Council or Council discussions which may affect it. However, the situation and voting rights of the UK elected MEPs is open to debate.

Unless expressly otherwise agreed, the Treaties would cease to apply to the UK from the date of entry into force of the withdrawal agreement or two years after the withdrawal notification if there is no agreement (for example, if the negotiations become protracted due to disagreement on the terms, or if there is no internal agreement within the Council (qualified majority), or at the European Parliament (simple majority)).

SPECIFIC IMPLICATIONS FOR BUSINESSES

Trade

Should the UK leave the EU, this would impact its trading of goods and services, both with the EU and with the rest of the world. Such impact would substantially differ depending on the level of integration that the UK will be able to maintain with the Union.

In the case of a Brexit, an important distinction is to be made between trade with the EU and trade with other countries.

As regards the trade relations with the EU, Brexit would impact the free movement under which goods circulate without any barriers within the EU Single Market. The withdrawal agreement would need to include the terms according to which the UK would eventually keep all or most of the trade benefits it currently enjoys as part of the EU Single Market.

The UK would have the choice to join the European Economic Area (**EEA**) at the same time it leaves the EU, in practical terms, remaining a part of the Single Market (as is the case with Norway). The disadvantage of this option is that the UK would be subject to EU law and regulation without being able to influence its drafting. For instance, the need of the UK to secure access to the EU market for its cars or food will make it necessary to still comply with the European regulation in those sectors, but not be part of any related negotiations on such regulation.

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Alternatively, the UK could include in the Withdrawal Agreement a bilateral arrangement with the EU similar to the one the EU has with Switzerland, which is not a member of the EU or EEA, but enjoys tariff-free access to the EU Single Market. However, the Swiss model is not easy to replicate — the EU and Switzerland have signed over 120 bilateral agreements, including a free trade agreement in 1972 and two major series of sectoral bilateral agreements that aligned a large portion of Swiss law with that of the EU at the time of signing. For many, these agreements have created a complex and sometimes incoherent network of obligations, which are not easy to sustain.

In addition, any preferential access to the Single Market could also trigger the intervention of other world trade partners of the EU, which could challenge this preferential treatment under the most-favoured-nation principle of WTO law.

Should the UK not be able to secure preferential access to the EU Single Market, its commercial relations with the EU will be governed by the WTO rules, which are not as wide in scope as the four freedoms of the Single Market.

As regards trade with non-EU countries, Brexit would impact several free trade agreements that the UK has benefited from as being part of the EU, including the ones with Korea, Chile, Mexico and South Africa. The ability of the UK to maintain the trade benefits negotiated for such a large trade zone — and in particular, the reduction of trade barriers — would largely depend on the not-easy legal interpretation of its rights as a remaining party to those agreements independently and in its own right, after having left the EU. Perhaps more significantly, the UK would be excluded from the benefits derived from any future agreements to be entered into by the EU, including TTIP, and further agreements with ASEAN, India or Singapore.

So, although the UK would enjoy more freedom in negotiating its own new bilateral trade treaties, it could compromise its bargaining power, as the EU as a whole currently represents one of the biggest and most powerful trading blocs in the world.

Financial Services

Much of the regulation of financial services in the UK is governed by EU law. This includes the regulation of banks, broker-dealers, insurers, insurance intermediaries, fund managers and payment services providers. Therefore, a Brexit would mean that financial institutions with operations crossing UK and EU borders would become subject to a new regulatory regime. The precise implications of a Brexit will depend on a variety of factors, including the arrangements that the UK implements to govern cross-border business between the UK and the remaining countries of the EU and the extent to which the UK government chooses to retain legislation that is based upon EU law.

An important element of the EU financial services regime is "passporting". Passporting is the exercise of the right by firms authorised under an applicable EU financial services directive to carry on activities in another EEA member state, on the basis of their home state authorisation. Their activities can be conducted through a branch in the host member state or on a cross-border services basis.

Many firms have adopted a business model based upon passporting to conduct their EU-wide operations. Should a Brexit result in the passporting regimes ceasing to apply in relation to business conducted into and out of the UK, firms in the UK and the remaining EU would need to consider whether to operate distinct authorised entities in both the UK and EU. Some non-EU financial institutions, which have established subsidiaries in the UK as a base from which to passport into the EU, might need to consider whether to move their base elsewhere. However,

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much will depend on the extent to which arrangements can be implemented to replicate passporting between the UK and EU, including whether the UK will be part of the EEA and able to participate in the arrangements that facilitate the cross-border provision of financial services between EEA member states.

Apart from strategic implications for the structure of EU business operations, a Brexit would trigger a host of practical implications for how financial institutions operate their businesses. For instance, where financial institutions distribute their products in the UK and elsewhere in the EU, they would need to review product terms, distribution agreements and marketing literature to consider whether these need to be amended or replaced as a result of a potential regulatory separation.

Employment Law

Although much of the UK's current employment law framework derives from the EU, it is generally thought unlikely that the UK's exit from the EU would result in significant legal changes, at least in the short term. There are several reasons for this.

First, the UK government would be concerned about the impact on its economy if sudden, wholesale changes to well-established employment principles were to be introduced at once. This would create a period of uncertainty for businesses at a time when economic confidence is already fragile. Many employment rights that originated at EU level, such as paid holiday or the right not to be discriminated against, are generally considered to be "good things". Even TUPE is now generally accepted (as shown by the recent government consultation on proposed changes) and many commercial agreements have been priced, drafted and signed on the basis that it applies. The government may identify a handful of less popular pieces of legislation which it considers could be removed without too much disruption, such as the Agency Workers Regulations 2010 and even the limits on bankers' pay contained in CRD IV, but it will be reluctant to implement a wholesale purge of any laws that have ever come from the EU.

Second, even if the UK leaves the EU, the desire to maintain some sort of free trade agreement with the EU (either by joining the EEA or negotiating bilateral agreements) will mean that the UK is still likely to be required by the EU to maintain minimum standards of employment protection to prevent the UK being able to undercut EU states through lower employment standards. Although the UK may be able to negotiate certain exemptions from the full range of EU laws, current EEA states (Norway, Iceland and Liechtenstein) are obliged to accept the majority of EU regulations without being part of the EU decision making process, and the UK is unlikely to be much different if this is the path it chooses to follow. This would also apply to free movement of persons, which is an integral part of the EEA agreement.

Intellectual Property

A possible Brexit would raise several complex legal issues in the field of intellectual property and related rights, both in terms of the applicable rules and in relation to the means for their enforcement. We refer here to four areas: patents, trademarks, copyright and the protection of trade secrets.

On **patents**, the United Kingdom is a part of several international conventions unrelated to membership of the European Union. This is essentially the case for the Convention on the Grant of European Patents of 5 October 1973, or European Patent Convention (**EPC**). The EPC provides a legal framework for the granting of European

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patents via a single, harmonised procedure before the European Patent Office. None of this would be affected by the UK leaving the EU, as non-EU members are already part of this system, including Turkey and Albania.

However, because this system is complex and expensive, a large group of EU members, including the UK in a leading role, promoted a new European patent with unitary effect, or Unitary Patent: one single title with one single registration and payment and a unified enforcement method under a unified court mechanism. This was viewed as being positive for SMEs and small innovative companies. Should the United Kingdom cease to be a member of the EU, its businesses would be excluded from the Unitary Patent system, unless a complex tailor-made solution can be agreed in the Withdrawal Agreement (including recognition of the jurisdiction of the Court of Justice of the EU in this matter).

Copyright remains an essentially territorial matter: titles and rights are created and enforced on a country-by-country basis, supplemented by several applicable international conventions that would not be affected by a Brexit. However, UK copyright legislation is today the result of implementing the EU Copyright Directive; and whilst the UK could keep that legislation internally and amend its laws in accordance to changes at an EU level, it would not be part of the EU internal negotiations to reform and modernize it and the UK's copyright legal system would not have the final enforcement of the Court of Justice of the EU.

In the field of **Trademarks**, there are currently two parallel legal schemes. A UK Trademark registration protects rights in England, Wales, Scotland and Northern Ireland. There is also the so-called Community Trademark (EU trademark registration), which protects trademark rights in the 28 member countries of the EU with a single title, and a single enforcement mechanism. It is the usual cost-effective choice for businesses currently operating across the single market. A new Directive and a new regulation on EU trademarks were approved at the end of 2015. The new rules modernise the Community Trademark system in the Union as a whole and adapt it to the Internet era, while preserving the complementary relationship between the European Union trade mark system and national trade mark systems.

In the case of a Brexit, the UK would have to negotiate with the EU, as part of the Withdrawal Agreement a mechanism to remain part of the Community Trademark system. Without this, all companies operating across Europe would need a double trademark registration: one for the UK and one for the EU market. What would happen with Community Trademarks already valid would be the object of any Brexit negotiation.

A new EU directive on **know-how and trade secrets** is expected to be approved early in 2016. Its objective is to put companies, inventors, researchers and creators on equal footing through discouraging unfair competition, and facilitating collaborative innovation and the sharing of valuable know-how. Should the UK leave the EU, the implementation of those new rules in the UK legal system (and thus, for the UK to have the same new, strong standards in this area) would be an independent decision of its Parliament; and the interpretation and enforcement of those rules would be limited to UK courts.

Dispute Resolution

As a result of its EU membership, the UK is subject to harmonised rules about the enforcement of judgments. The Brussels I Regulation regulates the recognition and enforcement of civil and commercial judgments across member states. It achieves this by setting out general rules governing cross-border jurisdiction disputes. Other European regulations in this area are Rome I, which allows contracting parties in a civil or commercial matter to

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choose the law that will apply to their contract; and Rome II, which achieves the same result for non-contractual cases.

Without these regulations, matters would be dependent on domestic rules of law in relevant countries, which can create uncertainty and disputes through a lack of harmonisation, as well as potential difficulties in the enforcement of legal rights and obligations including debts.

The position might be mitigated by means of two existing international conventions: the Lugano Convention has similar provisions to Brussels I, and applies to EEA and EFTA countries; and the Hague Convention on Choice of Court Agreements, to which all EU member states (bar Denmark) and (currently only) Mexico are bound. Of course, that begs the question whether the UK wishes to mirror existing arrangements or negotiate something afresh.

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[1] Section 1(3) of the Act
[2] Section 6 of the Act
[3] Section 7 of the Act

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