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In the aftermath of the UK's decision to leave the European Union, shockwaves continue to reverberate across both the financial markets and the political landscape. Here, Lord Jay of Ewelme, former British ambassador to France and former head of the Foreign and Commonwealth Office, joins Clifford Chance experts to discuss the legal and commercial realities of the UK moving towards Brexit.

On 23 June, the UK population defied predictions and voted to leave the European Union, with 52% of the more than 32 million people that voted opting for Brexit. While the polls had always suggested a close-run race, and businesses had been contingency planning for months, the result came as a surprise. The markets plunged into chaos and both of Britain's major political parties were quickly beset by resignations and leadership challenges.

Some of the questions that have been at the heart of discussions in the UK, Europe and around the world concern the mechanics of Article 50 – the part of the Lisbon Treaty that the UK must invoke in order to set in motion the formal legal process to withdraw from the EU – as well as how exit will be achieved, how market disruption might be minimised, and how the UK can maximise its market access going forward. The answers to these questions give us a glimpse as to the future of the UK economy, the UK's relationship with the EU, and its position in the world.

Negotiating Brexit

Lord Jay of Ewelme said that, despite the widespread calls for a second referendum, the only safe assumption is that 'no means no' and, within three to five years, Britain will leave the EU on terms still to be negotiated.

He supports the government decision to hold fire on invoking Article 50 until later this year, giving the new Prime Minister, Theresa May, time to take stock, and the civil service the opportunity to form a negotiating team, before starting the clock on its two-year negotiating period.

The government will then have to decide the basis on which it wishes to enter negotiations with the EU. Lord Jay said: "I think that the best outcome for the UK is to remain in the single



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Lord Jay of Ewelme

market – I think that’s best for business and best for our service industry, but it comes at a cost.”

One cost is a lack of influence over the various directives that will be negotiated by the other 27 member states and which Britain will have to sign up to. Others would be a – possibly quite substantial – budgetary contribution, and free movement of labour.

It is here that the economic imperative of the single market conflicts with the political reality, which is that the British people voted against freedom of movement. “How is that to be solved?” said Lord Jay. “If one is looking optimistically, maybe within the other 27 states there is going to have to be a rethinking of free movement because of the difficulties that have arisen over the last few months, and the circumstances that led to free movement being part of the four freedoms in the first place maybe no longer apply. So there could be some change by the 27 to the free movement rules, and the UK could then sign up to a single market with different rules to those that currently apply.”

Were that not to be the case, the alternatives look far less palatable, ranging from the Canada option, which allows for some access to the single market without such things as passporting for financial services, to plain vanilla World Trade Organisation membership. “The latter seems to me to be an option only if we are pushed into it because we haven’t managed to get a negotiation on anything else,” he said.

It is clear that the negotiations will be lengthy and complex, with all member states vigorously defending their own interests. For the UK, as the world’s sixth largest economy, there will be implications for its global standing. It will remain a member of the United Nations Security Council, of NATO, the G7 and the Commonwealth, and as such can maintain its position as an international power. In the future, the United States may build stronger relationships with European powers in France and Germany, ahead of the UK, but any actions taken by the EU will lack the muscular foreign policy input that the UK can provide.

Lord Jay concluded: “We have huge assets going for us, and I hope that we will be able to exert them and continue to play a significant role in the world, even if that may be a different one.”

The legal landscape

While much of what the UK is now embarking on with respect to Brexit is both uncertain and hypothetical, there are a few legal and procedural points to note. The negotiations will be a complex process, but Article 50 of the Lisbon Treaty provides for a very simple withdrawal mechanism, stating “Any Member State may decide to withdraw from the Union in accordance with its own constitutional requirements.” It goes on: “A Member State which decides to withdraw shall notify the European Council of its intention ... the Union shall negotiate and conclude an agreement with that State.”

That agreement is negotiated on behalf of the Union by the Council, acting by a qualified majority, after obtaining the consent of the European Parliament.

Article 50 has only been in force since late 2009 and has not yet been tested, but once it is triggered it allows for a two-year period of negotiation, which may be extended if all member states agree. The point at which the UK invokes Article 50 is in the hands of the UK government. Michel Petite, avocat of counsel in Clifford Chance's Paris office and a specialist in European Commission policies, said: "The 27 have sent a message that the UK is right to take a little bit of time before invoking Article 50, but there will be no formal or informal negotiations until that letter is signed."

Once the negotiations begin, two key issues will need to be addressed: the financial links between the UK and the EU will have to be untied, and the situation in which the UK will be left vis-à-vis third countries will have to be ironed out. The first of these involves a maze of complex relationships and will likely be acrimonious, while the latter concerns the EU's ties with 50-plus countries of the world through various types of trade agreements. Many of those are purely commercial arrangements between the EU and third countries, which will no longer hold when the UK leaves the EU.

On the other hand, many trade agreements include provisions that are more political, which refer to values, and talk about

cooperation on foreign policy, security and so on. Those trade provisions are described as 'mixed', because they imply both an obligation on behalf of the union, and on behalf of the member state. Petite said: "It will therefore be necessary to find an agreement on each of these, requiring extremely fine surgery to be carried out on those more than 50 agreements to establish what exactly falls when the UK leaves, and what doesn't."

He added: "People in the Commission are already nervous about this issue of trade agreements with third countries, at the idea that some significant country, which is not necessarily friendly, could challenge the entire agreement between the EU and that third country on the basis that the UK is no longer a member of the EU, so the circumstances have significantly changed and that agreement needs to be reviewed."

During the withdrawal negotiations the UK will remain a member of the EU, and so EU law will



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Michel Petite, Avocat of Counsel, Clifford Chance, Paris

still stand in the UK. That means new European laws will be negotiated and passed, and will apply to the UK, and that the Luxembourg court could rule that the UK has infringed European law and the UK must abide by its decision.

The relationship between the UK and the EU after exit will have to be the subject of another agreement, and EU law compels that that agreement cannot be negotiated until the UK has become a third country and left the union. Petite said: “Of course there will be a lot of discussion about the post-Brexit period and the member states and the Commission will need to have a view, but there will have to be two treaties: the withdrawal treaty will have to be followed by a second agreement governing the EU’s new relationship with the UK.”

That second treaty will require ratification by all 27 member states, which may not be easy to achieve, and so the process could be extremely lengthy.

Finally, Petite highlighted a misunderstanding about the single market, saying it is much more than simply a free trade zone. The single market allows goods and services to freely circulate because all originating countries are compliant with a single set of standards. So in order to remain in the single market, the UK must remain compliant with existing EU legislation, and must comply with new

EU legislation, and it must also remain answerable to the court that is responsible for enforcing those standards.

Commercial realities

Of all the options open to the UK in terms of its ongoing relationship with the EU post-Brexit, the so-called Norwegian option appears to be most popular with those that campaigned for the Leave vote. Norway has access to the single market, through the European Economic Area (EEA) and the European Free Trade Agreement (EFTA), but it has to comply with all its rules, representing a severe constraint on its autonomy as it has no say in the making of those rules. It also has to accept free movement of people, and has to make budgetary contributions, all of which seem to be exactly what the people of the UK voted against in the referendum.

An alternative may be that the UK could sign up to freedom of movement to come to work, but not freedom of movement to come to look



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Phillip Souta, Head of UK Public Policy, Clifford Chance, London

for work. That proposal has been rebuffed by people on the Continent, according to Phillip Souta, head of UK public policy at Clifford Chance in London, but could yet form a key tenet of the UK's negotiating position.

In the meantime, short term post-referendum issues have emerged for corporate treasuries. Financial institutions and corporates are already grappling with the impact of extreme volatility in the currency markets, creating particular issues for those with revenue streams in one currency and borrowings or trade liabilities in another. Companies with collateralised currency hedges could be required to post extra collateral to cover market exposures that could defeat existing lines of credit.

When it comes to contracts, businesses are advised to consider whether there are any terms in their contracts that could be triggered if the UK leaves the EU, such as illegality or material adverse change clauses, and to plan accordingly. "Illegality may become an issue as people stop being able to do what they were able to do under single market rules," said Souta.

There are many unknowns, and the EU could yet change beyond recognition while the UK negotiates its exit: "The idea of a new settlement, the like of which we don't see today, is a real possibility," said Souta. "In two years, it may be that the EU is something quite different from what we see today, that the UK could be on the peripheries of, or even join."

The only thing that is clear is that the apparently binary choice of Leave or Remain masked a much more extensive range of options.

Jessica Gladstone, Clifford Chance public international law partner, said: "The UK will now be deciding what it wants to do, and UK business must feed into that and explain what a new legal framework needs to look like in order for UK business to function as effectively as possible in this new world order."



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Jessica Gladstone, Partner, Clifford Chance, London

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