SLAUGHTER AND MAY

Brexit Essentials: The legal and business implications of the UK leaving the EU

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If the UK votes to the leave the EU on 23 June 2016, there could be significant consequences for businesses and financial markets in the UK, the EU and even globally. The precise impact of a "leave" vote depends on the form that the exit would take - a point that is yet to be decided.

This is the fifth in a series of briefings covering the essential aspects and implications of the UK's referendum on EU membership. This edition discusses the implications on specific areas of law and business if the UK were to leave the EU.

The legal and business impact of Brexit will depend on the strategy that is adopted for the UK's future relationship with the EU. The referendum question will decide whether the UK will remain in the EU, but will not determine the model for exit. The most commonly proposed models for the UK's post-Brexit relationship with the EU are:

i. the 'Norwegian model', under which the UK would leave the EU but join the EEA and EFTA, alongside Iceland, Liechtenstein and Norway, accepting the principles of free movement of goods, services, capital and workers in exchange for single market access;

ii. the 'Swiss model', by which the UK would leave the EU and join EFTA but not the EEA, negotiating a series of bilateral agreements with the EU to secure (some) single market access; and

iii. total exit from the EU and the EU single market, either relying on the rules of the World Trade Organisation ("WTO") to continue trading with the EU or seeking to negotiate a new free trade agreement (similar to that recently negotiated between the EU and Canada).

The pros and cons of these alternatives to EU membership are discussed in detail in the second edition of this series of briefings.

Regardless of the exit strategy, there are some areas of EU law that would continue to have an effect on UK businesses. For example, UK companies doing business in the EU would need to continue to comply with EU product standards and EU competition rules. Under any exit model, the UK would continue to operate within globalised markets. This would require the UK Government to balance the temptation to create less stringent or different regulations, in order to attract non-European companies to the UK, against the need for an ongoing relationship and consistency with Europe, and with European companies and investors.

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Advocates for Brexit have argued that upon leaving the EU, the UK will be free from the shackles of EU-derived regulation. The EU's influence will not, however, instantly be stripped from the statute book – it will depend on what the UK Parliament, Government, courts and sector regulators choose to do with the existing UK laws that are derived from more than 40 years of EU membership. The UK Government's ability to effect material amendments, or to remove laws entirely, will depend on the Brexit model adopted and other external factors.

For further detail and advice on the implications of Brexit for your business and how Slaughter and May can assist you in contingency planning, please contact your usual Slaughter and May advisor.

To read earlier editions of the briefings in this series, please see:

1. Brexit Essentials: UK proposals for EU reform
2. Brexit Essentials: Alternatives to EU membership
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1. M&A

M&A laws and regulations are unlikely to be materially affected by Brexit, but from a commercial perspective it would present both risks and opportunities depending on the industry sector

M&A laws and regulations are unlikely to be materially affected, at least initially, by Brexit, because the influence of EU-derived law and regulation is minimal, the UK's existing framework (broadly) works, and there is little appetite for material change.

In the public sphere, the UK Takeover Code (the "Code") gives effect to the EU Takeovers Directive, but cannot be said to derive from it; on the contrary, the EU Takeovers Directive was heavily influenced by the Code (as it was at the time the Takeovers Directive was drafted). The Code has evolved, and continues to evolve, more or less independently of Europe, in light of market conditions and the views of City of London market participants, including the UK Takeover Panel. The nature of the Code's creation and evolution mean that it is broadly accepted and respected as an appropriate framework for public M&A in the UK. It is not therefore likely that there would significant changes to the Code as a result of Brexit (under any possible exit model).

Over time, the Code could be expected to adapt and evolve relatively rapidly in light of prevailing market conditions in both the UK and globally, as well as shifting regulatory sands on foreign shores, including in Europe. For example, if the UK were to leave the EU and seek to encourage increased foreign investment and ownership, whether in response to relaxations of the EU Takeovers Directive in the UK or in order to establish closer ties with other countries such as the US, the Code could be expected to adapt (and be relaxed) to reflect this.

This ability to adapt rapidly could be even more important post-Brexit than it is today, depending on the extent to which the UK's ties with Europe are loosened. Adaptability will be critical in a total exit scenario, albeit perhaps less critical (and less possible) if the UK adopts the Norwegian model and commits, as would be required under the current EEA Agreement, to the EU Takeovers Directive.

In the private sphere, EU-derived law and regulation has very little influence on the UK's M&A rules and so Brexit is likely to have very little effect on domestic transactions. However, the rules governing and enabling cross-border mergers between UK companies and companies incorporated in other EEA States could be affected. Although the rules are only infrequently used, they do provide greater optionality for UK companies and there could therefore be some benefit in their retention. If the UK were to leave the EU but join the EEA, the default position (in the absence of a renegotiation of the EEA Agreement) would be that the EU Cross-Border Merger Directive would continue to apply. Otherwise, both under the Swiss model and in the event of a total exit, the UK would either need to agree with the EU that the directive remained applicable or negotiate equivalent arrangements bilaterally with individual EU Member States.

From a commercial perspective, under any exit model, Brexit would likely present both risks and opportunities. Its effect on M&A will vary between companies and between industries, in some cases stirring activity, in others encouraging calm.

2. Corporate law

Post-Brexit, there will almost certainly be some EU-derived corporate laws and regulations that the UK Government would prefer to amend or remove – but external factors may prevent it from doing so

European law and regulation has a much more significant influence on other areas of UK corporate law. The UK Government's view of this influence has been mixed:

- A number of EU directives have been warmly welcomed and implemented, such as those covering accounting rules, money laundering, market abuse and transparency.

- A number of EU directives were broadly accepted in principle, with there being varying degrees of consternation as to the detail of the implemented laws (focused oftentimes on perceived unnecessary red tape and/or gold-plating). These include the Markets in Financial Instruments Directive ("MiFID"), the Solvency II Directive and the Prospectus Directive.

- Other EU directives and rules affecting directly or indirectly UK corporate law have been (and are being) opposed, including the Alternative Investment Fund Managers Directive ("AIFMD"), European Securities and Markets Authority's short-selling restrictions and the proposed financial transactions tax.[1]

Post-Brexit, there will therefore almost certainly be some EU-derived corporate laws and regulations that the UK Government would - in the absence of external factors - prefer to amend materially or remove entirely. The UK Government's ability to effect material amendments, or to remove swathes of this legislation entirely, will depend on the exit model adopted and other external factors.

Under the Norwegian model, the default position is that the UK would be required to comply in full with almost all of the EU-derived corporate laws and regulations listed above, including the Prospectus Directive, MiFID and AIFMD, as they are incorporated into the EEA Agreement. The UK Government could look to negotiate dispensations from the EEA Agreement, albeit this would involve the EU accepting what would effectively be a hybrid of the Norwegian and Swiss models. Under the Swiss model, or in the event of a total exit, the UK would only be required to comply with the EU-derived corporate laws and regulations if it agreed to do so in the negotiated exit arrangements with the EU.

Under any exit, the UK would continue to operate within globalised markets. The UK Government would be mindful of the need to attract non-UK issuers and investors, from both Europe and the rest of the world. It would need to balance the temptation to create less stringent regulations to attract more non-European companies to the UK against the need for an ongoing relationship with European companies and investors.

For example, relaxing the UK's Prospectus Rules may initially seem attractive as a means of making the London Stock Exchange more readily accessible and public offers of shares less burdensome. However, a UK prospectus issued under relaxed rules would then not satisfy the European requirements, which could

[1] The implications for a number of these rules are covered in greater detail in the financial services and insurance section and the Real Estate section of this briefing.

give rise to complications if the issuer in question had, or was targeting, a European investor base. Unless the EU or the relevant Member States were prepared to accept prospectuses produced under revised UK rules, the issuer would have to exclude European investors from its public offer or produce an EU-compliant prospectus. The EU is unlikely to accept a prospectus that differs materially from the EU-compliant norm.

Such external considerations would therefore seem likely to cool any burning desire, and restrict the UK Government's ability, to deviate materially from the existing (and future) EU corporate rule book.

The impact of Brexit on disclosure obligations in annual reports for public companies is discussed in the Financing section of this briefing.

3. Financing

Debt market participants should continue to monitor the likely effect of Brexit on debt market conditions and consider whether any Brexit-related prospectus disclosure is required. In time, it may be necessary to consider the terms of material financing contracts in further detail. Over the longer term, the extent to which the EU will be driven to implement a capital markets union without the UK's influence is unclear

From a practical perspective, it would seem disproportionate for debt market participants to undertake detailed due diligence of financing arrangements at present given the current range of uncertainties as to the form that a UK exit from the EU might take. Cautious monitoring is likely to be the most pragmatic approach in the near term, although the situation should be kept under review.

This section considers some short- to long-term considerations which those active in the debt markets should keep under review as the situation evolves.

Short- to medium-term considerations

Debt market conditions

Whatever the result, the referendum is likely to provoke some uncertainty and volatility in the debt markets, which are invariably sensitive to political and economic events. Lenders may consequently be less willing to lend and the cost of borrowing may increase. A "leave" vote and the protracted divorce period that is anticipated may result in even greater uncertainty and volatility.

While at present there does not appear to be a visible negative effect on banking relationships or lender/bondholder behaviour (aside from general uncertainty about the outcome and impact of the referendum), lenders' response to UK borrowers and their debt trading patterns will be one to monitor as the situation evolves.

Disclosure

Issuers that are required to publish disclosure, whether in the context of a prospectus in relation to new offers or admissions of securities or in the context of an annual report in relation to public companies, should consider the extent to which a Brexit risk factor should be disclosed. Currently, Brexit risk factors tend to be relatively short, and often still contained within wider political risk factors, although the trend is moving towards more specific disclosure. In the event of a "leave" vote, it may be worth going into further detail as the new arrangement between the UK and the EU becomes clearer.

Due diligence

Brexit is unlikely to frustrate or affect the enforceability of English law-governed financing contracts. In time, however, it may be necessary to review the terms of material financing contracts in further detail, for example events of default and termination events.

i. **MAC and force majeure.** It is unlikely that Brexit would constitute an event of default under a loan agreement based on the Loan Market Association's recommended forms. For example, they do not generally contain material adverse change or force majeure provisions that operate by reference to conditions in the financial markets, operating instead primarily by reference to the financial condition of the group (unlike some loan mandate letters). It is similarly unlikely that Brexit would trigger standard events of default or force majeure provisions in bond documentation. However, the precise terms of any particular financing contract should always be reviewed, and the specific circumstances taken into account (as lenders sometimes negotiate broader and more sensitive triggers). Bespoke events of default specifically addressing Brexit are unlikely while the debate as to what constitutes Brexit continues.

ii. **Increased costs.** Many banks in their financing documentation have the legal right to pass the costs of regulatory change (typically broadly defined) on to their borrowers. Even if for relationship reasons they are likely to be reluctant to invoke such a right, it remains to be seen what the regulatory effect of Brexit will be and how it will effect both UK and overseas banks lending into the UK.

iii. **COMI representations.** Some financing arrangements restrict relocation of the borrower, including a repeating representation or undertaking that the borrower's "centre of main interests" (an Insolvency Regulation concept) is its place of incorporation and location of its registered office. In those cases, if a borrower's Brexit contingency planning involves extensive relocation of its business and staff, there may be lender consent issues to consider.

Longer-term implications

Debt capital markets

Much of the legal and regulatory regimes underpinning debt capital markets and securitisation in the UK is derived from directives and regulations that apply to the entire EEA (rather than simply the EU), but not to EFTA. The extent to which these regimes would change upon Brexit would therefore largely depend on the exit model adopted. If the UK adopts the Norwegian model and joins the EEA, the underlying legal framework will change very little. If the UK does not join the EEA (i.e. under the Swiss model or any total exit model), the legal and regulatory framework that the UK creates will depend on a range of factors, including the extent to which the UK seeks to establish a regime that is considered equivalent to that in the EU; the extent to which the UK seeks to reflect global and international standards; and the extent to which the UK seeks to deregulate.

Capital markets union

One of the key political goals of the current European Commission is the creation of a new capital markets union, effectively completing the single market for capital. Given the position of the City of London and the UK's dominant financial services industry, the UK is one of the EU Member States that is most keen for capital markets union to progress. The reform package agreed upon by the 28 EU Member States in February 2016, to be implemented should the UK vote to remain in the EU, confirms the EU's commitment to completing the single market for capital and the EU *"will make all efforts to fully implement and strengthen the internal market"* (as discussed in the third edition of this briefing). In the event of a Brexit, the position of the UK within the capital markets union and the extent to which the rest of the EU is motivated to pursue the capital markets union will be an open question.

4. Dispute resolution

The UK may face the prospect of its court judgments becoming less effective across Europe. Businesses need to consider the possibility of additional disputes arising as parties seek to extract themselves from contracts that are no longer attractive if the UK is not part of the EU

The UK has built its reputation as one of the leading centres for international dispute resolution over centuries. The Commercial Court and the London Court of International Arbitration ("LCIA") helped parties to resolve their disputes long before the UK joined the EU and will continue to do so if the UK votes to leave the EU. Choice of English law and forum is already embedded in many contracts.

That is not to say that things will remain as they always have been. Brexit would create uncertainty and set in train long-term effects that are impossible to predict. EU businesses might question whether English judgments will be enforceable in their home state and whether English law will treat EU nationals fairly. Some of these fears may be fanciful, but the UK should not take its current privileged status for granted.

Uncertainty also breeds disputes. Parties might question their EU ventures (UK inbound and outbound) and seek creative ways to extract themselves from contracts they wish they had not signed.

If the UK leaves the EU, the extent to which the UK Parliament and the UK courts would be truly free to act independently of the EU would depend on the exit model chosen. For example, under the Norwegian model based on EEA and EFTA membership, the UK would nevertheless apply EU law to the extent that it has been incorporated into the EEA Agreement (with the EFTA Court as the final arbiter – which is bound to follow decisions of the Court of Justice of the European Union).

Jurisdiction and enforcement

As a member of the EU, the UK currently benefits from various Regulations and Conventions (principally, the Recast Brussels Regulation and the 2007 Lugano Convention[2]), which ensure that the courts of EU Member States and EEA-EFTA States (except Liechtenstein) apply common jurisdictional rules to determine when they will accept jurisdiction over a dispute and that a judgment given in one State will, subject to limited exceptions, be enforceable in all other participating States.

Post-Brexit, the UK would have to replace these arrangements or face the prospect of its courts' judgments becoming less effective across Europe. Without a replacement, international parties might be persuaded to nominate an EU Member State (rather than the UK) as the forum for their disputes if a pan-European judgment was important to them or, alternatively, switch to arbitration.

The alternatives range from the UK signing the Lugano Convention in its own right (as opposed to as part of the EU, as at present); signing individual treaties with EU Member States for mutual recognition and enforcement of judgments; or doing nothing. The first two options require the co-operation of other States and, while they are likely to be attracted to the idea of their judgments being readily enforceable

[2] Regulation (EU) 1215/2012 of the European Parliament and of the Council of 12 December 2012 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters (recast); The Lugano Convention on jurisdiction and the enforcement of judgments in civil and commercial matters (30 October 2007).

in the UK, they might seek to attach conditions to that agreement. Doing nothing would mean that an English judgment would be no more enforceable in France than it is at present in, say, New York. This would not be a complete disaster as international principles of comity ensure that friendly jurisdictions typically recognise and enforce each other's judgments, but the process is usually more expensive and less certain for litigants compared with the current intra-EEA regimes. One potential upside is that UK courts would once again be able to restrain (by way of anti-suit injunction) defendants that acted contrary to an exclusive jurisdiction clause by filing proceedings in an EU court.

Brexit would not affect the conduct of arbitrations with their seat in London, which are subject to the UK Arbitration Act 1996, nor the international enforcement of awards arising from those arbitrations, which is the subject of the New York Convention[3], an international instrument to which the UK (and all the other Member States of the EU) are parties in their own right independent of the existence of the EU. As noted above, there might be a shift towards arbitration in London (or elsewhere) if Brexit takes place and the UK does not find a way of ensuring that its judgments remain enforceable across Europe.

The effect of Brexit on pan-European remedies, such as cross-border injunctions, is discussed in the Intellectual Property section of this briefing.

Governing law

The issue of which law applies to contractual and non-contractual obligations in UK courts is at present determined by the EU's "Rome Regulations"[4]. Following Brexit, the UK could either fall back to the conflict of laws rules previously in force[5], or simply incorporate the Rome Regulations into UK law. Other EU Member States will continue to apply the Rome Regulations in the same way as they do now. The effect is therefore unlikely to be significant and all courts, whether in the UK or the EU, are highly likely to continue to uphold the parties' choice of law (be that English law or another law) and apply similar rules to determine what law should apply if the parties have not made a choice.

Substantive law

The UK will need to reassure citizens, businesses and foreign investors on how it intends to address those aspects of UK law that stem from the EU. Will it simply incorporate the substance of EU Regulations (for example, on health and safety, employment law and consumer protection) into UK law (as it might for an EC Directive)? Or will it exercise its new-found sovereignty to change the substance of the rules? If so, what changes will it make and will they discriminate against EU individuals or businesses that wish to do business with the UK (for instance, by restricting an individual's right to work in the UK and an employer's right to hire)? The detail inevitably will depend upon the relationship the UK is able to negotiate with the EU following exit. Current members of the EEA have to accept substantially all of the EU's laws.

3 Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 1958).
4 Rome I Regulation on the law applicable to contractual obligations ((EC) 593/2008), and Rome II Regulation on the law applicable to non-contractual obligations ((EC) 864/2007).
5 That is, the Contracts (Applicable Law) Act 1990 (which implemented the Convention on the Law Applicable to Contractual Obligations, opened for signature in Rome in 1980), or the English common law rules, which are based on the principle of party autonomy and that have influenced the development of legal systems around the world.

"In the UK [...] from 1997 to 2009 6.8% of primary legislation (Statutes) and 14.1% of secondary legislation (Statutory Instruments) had a role in implementing EU obligations, although the degree of involvement varied from passing reference to explicit implementation."

"The British Government estimates that around 50% of UK legislation with a significant economic impact originates from EU legislation."

House of Commons Research Paper, October 2010[6]

The uncertainty created by the referendum and subsequent period of upheaval might give rise to disputes as parties seek to extract themselves from contracts that are no longer attractive if the UK is not part of the EU. Parties can of course seek to set out in their contract that should happen in a post-Brexit world. However, given that the Brexit model remains undefined, it is impossible to pre-empt all issues that will arise and some issues will inevitably lead to disputes.

Brexit disputes

Parties looking to exit their contracts might, for example, claim that Brexit:

i. is a force majeure event giving rise to a termination right;

ii. frustrates the performance of contractual obligations, especially where it is argued that Brexit makes it impossible for a UK firm to do business in the EU (or vice versa) or at least on radically different terms. Under current EU legislation, a UK-authorised firm can carry out business in another EEA State so long as it meets the requirements of the single market directive under which it carries out its activities. Brexit may well mean that UK-authorised firms lose these "passporting" rights, and are denied the free access to EU markets that they previously enjoyed; and/or

iii. engages the "material adverse effect" provisions routinely included in commercial agreements, and which entitle certain parties to terminate.

A court's view of these disputes is likely to depend upon the context in which the contract was made: was Brexit foreseeable at the time of the contract? does the contract expressly anticipate Brexit-type events? or is membership of the UK essential to performance of the contract?[7]

6 House of Commons Library 'How much legislation comes from Europe?' research paper 10/62, 13 October 2010.
7 The effect of Brexit on financing contracts in particular is discussed in the Financing section of this briefing.

5. Competition law and State aid

UK companies doing business in the EU will not be able to avoid EU merger control and antitrust rules, but may find themselves subject to parallel UK and EU investigations

EU competition law is an effects-based regime that applies to the location where business is conducted, not where it is domiciled. To the extent that UK firms do business in the EU, they would therefore continue to be subject to EU competition rules even if the UK voted to leave the EU. Mergers, acquisitions and joint ventures that exceeded the relevant EU thresholds would continue to require merger control clearance from the European Commission. EU antitrust rules would also continue to apply to the behaviour of UK companies to the extent that the relevant conduct, agreement or practice has an appreciable effect on trade between EU Member States. Indeed, the highest individual antitrust fine issued to date by the European Commission was imposed on a company domiciled in the US[8], and the European Commission has intervened to block proposed mergers between two non-EU companies[9].

The UK's national competition laws are based on the EU competition rules, although in certain respects the UK has been a trailblazer and its regime goes beyond that of the EU (for example, the UK merger regime can review (and block) certain acquisitions of minority shareholdings, which the EU regime cannot). The UK competition authority (the Competition and Markets Authority or "CMA") is empowered to enforce the EU and UK competition rules. The Competition Act provides that the CMA and the UK courts must be consistent with EU competition law and with decisions of the EU courts, and have regard to decisions taken by the European Commission[10].

If the UK followed the Norwegian model by leaving the EU but instead joining the EEA, there would likely be very little effect on competition law and the State aid rules, as the EEA Agreement replicates the substantive competition rules of the EU. A practical change is that the EFTA Surveillance Authority, rather than the European Commission, would have jurisdiction to apply the relevant rules at supra-national level: it has the same enforcement powers as the European Commission in respect of conduct that applies to the EEA States[11]. However, it would be the EU, not the EEA States, that would decide what those rules are. If the EU were to make changes to the EU competition law rules, the UK would not have a seat at the table in deciding how those rules developed. This lack of influence in the legislative process for rules that have a direct effect in the UK would affect not just competition law but all EU laws incorporated into the EEA Agreement (as discussed in the second edition of this briefing series).

If the UK exited the EU, the EEA and EFTA entirely, the competition rules applicable in the UK would be determined entirely at the national level. Companies (of any domicile) that are active in both the UK and the EU would therefore lose the benefit of the European Commission's "one-stop shop", and could find themselves subject to parallel antitrust investigations in both the UK and the EU and having to file merger

[8] In 2009 the European Commission imposed fines of €1.06 billion on Intel for having abused its dominant position.
[9] For example, the proposed merger of US firms General Electric and Honeywell was blocked by the European Commission in 2001, despite being cleared by the US Department of Justice and 11 other jurisdictions.
[10] Section 60, Competition Act 1998.
[11] In practice, however, for merger control the jurisdictional thresholds have the result that the European Commission handles all cases: the EFTA Surveillance Authority has never carried out a merger control review.

control notifications at both the EU and UK levels. Under any total exit model, the caseload of the CMA could therefore be expected to increase significantly.

In such circumstances, it is to be expected that the UK Parliament would legislate to remove the requirement in the Competition Act for consistency with EU competition law and the ability of the CMA to apply EU competition law directly. However, given the (current) similarities between the UK's national competition laws and those of the EU, it may be that the UK courts continue to look to EU case law for interpreting questions of UK competition law. Parliament may also choose to amend certain aspects of the UK competition rules, and it would be free to diverge from the EU rules in doing so. This is not likely to happen in the short term, as the principles of competition law are widely accepted, but it is possible that over the long term there will be divergences in the development of the UK and EU competition law regimes. Businesses (both UK firms doing business in the EU and EU firms doing business in the UK) could therefore face practical issues with competition compliance (and increased costs of expanding their compliance policies) if the UK regime were to diverge significantly from the EU regime.

Brexit would also raise a practical issue regarding the protection of legal advice. Only advice given by external EEA-qualified counsel is privileged *vis-à-vis* the European institutions (i.e. it is protected from disclosure in an EU antitrust, merger control or State aid investigation). If the UK leaves the EU and does not join the EEA, advice from external UK-qualified counsel would cease to be privileged in the EU.

Antitrust rules

The UK's national laws prohibiting anticompetitive agreements and abuse of a dominant position are substantially the same as the EU rules, and it is not likely that they would change significantly upon Brexit.

At present, the European Commission takes jurisdiction over antitrust investigations where the relevant conduct had an effect on trade between Member States, including the UK. If the UK were to leave the EU, the European Commission and the CMA may have parallel jurisdiction to enforce the relevant competition rules, meaning that companies could find themselves subject to two investigations (and, crucially, facing two separate penalties) in respect of the same conduct – significantly increasing the burden on businesses with respect to time and costs.

"From the point of view of British businesses doing business in the EU, and foreign businesses doing business here, you are going to have much larger burdens on business from competition investigations and potentially increased fines."

John Fingleton, former Chief Executive of the Office of Fair Trading, 23 February 2016

A likely knock-on effect from Brexit would be on third party antitrust damages actions, which may threaten the status of the UK as a preferred forum for competition litigation. The current position under UK law is that third party follow-on actions can be brought once an infringement decision has been taken by the European Commission or the CMA (or a sector regulator with concurrent competition powers) in respect of EU or UK competition law. If the UK were to leave the EU, it is not clear if decisions taken by the European Commission would continue to have this status.

If the UK left the EU but did not join the EEA, litigating parties in the UK would not benefit from the Damages Directive[12], which provides that a final infringement decision by a national competition authority or national court in one EU Member State will constitute at least *prima facie* evidence before the courts of another EU Member State that an infringement has occurred – making it significantly easier for claimants to prove that they have suffered harm[13]. This may have a significant impact upon claimants' choice of London as a forum for follow-on damages actions.

The Damages Directive also provides that national courts cannot at any time order a party to disclose leniency statements or settlement submissions[14]. This is of significant benefit to companies facing antitrust investigations, as it means that submissions outlining a company's involvement in anticompetitive conduct in exchange for immunity or leniency in fines cannot be disclosed as evidence to third parties seeking damages in respect of that conduct. Such statutory protection of leniency documents is not currently a feature of the UK's national law – which, conversely, may redress the balance in increasing the attractiveness of the UK as a litigation forum for claimants. The Damages Directive has not yet been implemented into UK law; the deadline to do so is 27 December 2016. If the UK voted to leave the EU in the referendum, it is not clear whether the proposed changes to UK law on third party damages actions would go ahead.

Merger control

The EU merger control regime operates as a "one-stop shop", meaning that when the turnover thresholds are met at the EU-level, merging parties do not have to file separate notifications to the national competition authorities of the EU Member States. For large transactions where the merging parties make sales across the EU, this principle can significantly reduce the number of filings that are required.

If the UK leaves the EU and does not join the EEA, merging parties would be required to make two parallel merger control filings for transactions that met both the EU and the UK jurisdictional thresholds – with the concomitant increase in time, legal fees and filing fees. However, for large cross-border transactions that require multiple merger control filings around the world, the addition of an extra notification requirement may not be overly burdensome. Nonetheless, multiple notifications increase the risk that the different competition authorities could produce conflicting decisions.

Notification of mergers in the UK is voluntary, although the CMA can "call in" transactions and open an investigation on its own initiative or if it receives a third party complaint. However, post-Brexit, a transaction that is notified to the European Commission is unlikely to avoid the CMA's notice if it carries a risk of anticompetitive effects in the UK.

State aid

Aid granted by EU Member States that favours certain undertakings or the production of certain goods, thereby distorting competition, is prohibited unless it is approved in advance by the European Commission.

[12] Directive 2014/104/EU of 26 November 2014 on certain rules governing actions for damages under national law for infringements of the competition law provisions of the Member States and of the European Union (the "Damages Directive").
[13] *Ibid*, Article 9(2).
[14] *Ibid*, Article 6(6).

The rationale behind these rules is to prevent protectionism - which would be contrary to the principles of the single market - and stop anti-competitive market distortions arising through government support. These rules are enforced in the EU exclusively by the European Commission; there are no equivalent rules at national level. The EEA Agreement contains broadly similar State aid rules, although they are enforced by the EFTA Surveillance Authority in the EEA States.

If the UK left the EU and did not join the EEA, the State aid rules would cease to apply to the UK[15]. The UK Government would therefore be free to provide funding to UK businesses as it saw fit and would have the flexibility to support "national champions" if it wished to do so. UK businesses in sectors that have been or could be recipients of State funding could therefore be at an advantage, as State aid would not need to be approved by the European Commission before it was awarded, and there would be no risk of having to pay back State aid found to be unlawfully granted.

These advantages would, however, need to be balanced against the loss of protection for UK businesses against anti-competitive support given to their competitors. There are currently no alternative rules in the UK governing the provision of State support to private businesses (although there are more general WTO rules in relation to State subsidies that apply to all WTO members). UK businesses would also lose the ability to complain to the European Commission about State aid granted to their European competitors by EU Member States. If it left the EU and did not join the EEA, the UK would lose its rights to appeal European Commission decisions approving State aid to EU businesses, which could negatively affect UK competitors.

[15] If the UK exited the EU but, like Switzerland, joined EFTA and negotiated some market access through bilateral agreements, it may be the case that rules relating to State aid formed part of the negotiated package. There are prohibitions on State aid in certain sectors in the bilateral agreements between Switzerland and the EU; however, there is significant disagreement between Switzerland and the EU on the extent to which these apply, and the available sanctions. As a result, Switzerland has no specific legislation regarding State aid, and except in the air transport sector no Swiss authority is explicitly empowered to enforce State aid rules at national level.

6. Pensions and employment

Brexit is likely to lead to pressure to repeal or amend certain areas of EU social and employment legislation, such as the Working Time Directive. However, there is unlikely to be a major overhaul of existing employment and pension legislation in the short term

There have been controversies around EU legislation in the field of employment law. Some argue that social and employment legislation should not be within the competence of the EU. Others argue that there is a clear and direct link between the internal market and social and employment legislation; by setting minimum requirements, the EU ensures that businesses in the internal market compete within the same basic framework.

It has been argued by some business organisations that EU social and employment legislation imposes an unnecessary layer of red tape[16]. In general, there has been less debate concerning pension legislation deriving its roots from the EU, given that the EU's influence has on the whole been less significant in UK pension matters.

Given this background, Brexit is likely to lead to pressure to repeal or amend certain areas of EU social and employment legislation that have been transposed into UK law. However, at least in the short- to medium-term, it seems unlikely that there would be a major overhaul of existing employment and pension legislation as a result of Brexit. Any changes would likely not take place immediately but over time.

The type and extent of any changes will of course depend on which political party is in power in the UK and the form that Brexit takes. For example, if the UK follows the Norwegian model and joins the EEA it would, as part of its EEA membership, continue to remain subject to the bulk of EU legislation. Many UK laws that have emanated from the EU have become so widely accepted that any government would be reluctant to introduce changes to them. Changes to "gold-plated" legislation (i.e. UK legislation that exceeds the requirements of an EU directive) are unlikely to be made solely as a result of a Brexit.

Working time and agency workers

"With regard to the working time directive, the government wants to ensure that it promotes long-term, sustainable growth and labour market flexibility […] Our priorities are to retain the individual's right to opt-out of the 48-hour limit in weekly working time and to address problems caused by European Court Judgments on on-call time, compensatory rest and holiday pay."

David Lidington, UK Minister for Europe, September 2015

[16] The UK's goal of reducing the burden on businesses and cutting red tape was also reflected in the reform package agreed in February 2016 that will take effect if the UK votes to remain in the EU (as discussed in the third edition of this briefing).

"Given the very significant costs of complying with the EU directive, we should be bold in stripping out needless administration that threatens hiring and does nothing to benefit temporary workers."

Neil Carberry, CBI Director of Employment & Skills, October 2012

Following Brexit, the UK regulations giving effect to the Working Time Directive could be an area that the UK Government would wish to amend in order to introduce increased flexibility and discretion for employers, where recent decisions by the Court of Justice of the European Union ("ECJ") have made this area complex. It is likely that the widely used "opt-out" right would be retained. However, holiday pay rules could be relaxed, allowing employers to reach their own decisions on the appropriate level of pay and the ability of employees to carry over leave. However, working hours, sick pay and holiday pay and allowance are typically set out in individual employment contracts and therefore the effect of any changes made in this area may be reduced as a result of contractual terms.

The UK Government may also consider introducing a similar level of flexibility to the Agency Workers Regulations 2010 to reduce the costs associated with agency workers and increase the number of employers hiring agency workers.

Anti-discrimination laws

"At the moment, there are strict limits on the awards that a tribunal can give in respect of claims for unfair dismissal arising from ordinary employment law. When the claim for unfair dismissal is based on discrimination, however, an unlimited amount of damages can be awarded. That is now leading to all sorts of farcical situations."

Christopher Chope, Conservative MP, June 2011

Given that the fundamental principles in the Equality Act 2010 are so enshrined in UK law, it is unlikely that this piece of primary legislation will undergo any form of radical change. The Equality Act 2010 itself stems from EU legislation, as it implements the principle of equal treatment for men and women regarding employment, vocational training and promotion, and working conditions as set out in Equal Treatment Directive[17].

In light of concerns such as those raised by the CBI in 2013 regarding the threat that lengthy delays in tribunal claims posed for firms[18], the UK Government may consider the introduction of a cap for damages awarded in discrimination claims. The introduction of such a cap would serve to bring such claims in line with unfair dismissal claims, where compensatory awards are subject to a statutory cap of £78,335. The Tribunals (Maximum Compensation Awards) Bill 2010-12, if passed, would have imposed a £50,000 cap on compensation awards. This Bill was debated briefly on 17 June 2011 in its second reading and was subsequently adjourned. However, this may be an area for future reform.

[17] Directive 2006/54/EC of 5 July 2006 on the implementation of the principle of equal opportunities and equal treatment of men and women in matters of employment and occupation (recast).
[18] CBI report '*The right balance: delivering effective employment tribunals*', March 2013.

A further possible area for reform could be how pension benefits may be exempted from some anti-discrimination provisions. Currently, for instance, there is some uncertainty surrounding how guaranteed minimum pensions – namely, the minimum final salary benefits provided by certain types of pension schemes – are to be equalised between men and women, having regard to the historical difference in state pension age between genders.

TUPE

The Acquired Rights Directive was given effect in the UK by the Transfer of Undertakings (Protection of Employment) Regulations 2006 ("TUPE"). As with the Equality Act 2010, TUPE requirements have become a well-established part of UK employment law. The recent amendments made to TUPE in 2014 resulted from the UK Government's aim to remove unnecessary gold-plating when EU rules were implemented in the UK, and include clarification of rules relating to "service provision changes" and a longer time frame within which to provide employee liability information on a transfer.

"TUPE rules are essential to making sure that when a business is transferred from one company to another, it happens in a fair and efficient way."

Jo Swinson, Minister for Employment Relations and Consumer Affairs, September 2013

Following Brexit, the UK Government may seek to simplify the position for employers, which could lead to a lessening of restrictions surrounding changes of contractual terms post-transfer and a relaxation of information and consultation requirements. Further, in the context of collective redundancies the employer's obligations under the Trade Union and Labour Relations (Consolidation) Act 1992 could similarly be relaxed regarding to the duty to inform and consult in connection with a change of contractual terms.

The treatment of pensions under TUPE remains complex, and there is uncertainty around the scope of the occupational pension scheme exclusion, which may be an area for further reform or clarification by the UK Government following Brexit.

The Capital Requirements Directive and bonuses

In 2014, the UK Government withdrew its challenge to the cap on bankers' bonuses introduced by the Capital Requirements Directive. The UK viewed the directive as self-defeating, as it created incentives to raise salaries to mitigate the effects of the caps. Brexit could therefore see a move to remove the cap on bankers' bonuses introduced by the directive.

Family-friendly rights

Family-friendly rights in the UK, such as parental leave, have exceeded the necessary requirements under EU legislation. Such rights incur significant costs for employers, but UK employers may continue to promote such rights as recruitment and retention incentives. It is unlikely that the UK Government would introduce any significant change to these rights post-Brexit.

Cross-border pension schemes and the IORPs Directive

Many formerly cross-border pension schemes chose to cease operating cross-border as a result of the onerous requirement to be fully funded on their technical provisions at all times, introduced by the IORPs Directive[19]. While the proposals for a revised IORP Directive ("IORP II") have been published by the European Commission, IORP II fails to relax the funding requirements for cross-border schemes. Following Brexit, there is potential for these stringent funding requirements to be either relaxed or removed by the UK Government, and such changes may make these types of schemes more attractive and easier to manage.

"Not only is that one of the principles of the EU, it's the basis of any serious single market. The Norwegians, who eurosceptics admire, they accept the free movement of labour. They've got a bigger proportion of other EU nationals in their country compared with their own nationals than we have […] If you want to be in the single market, if you want to be a modern economy then the free movement of labour is essential, but free movement of labour shouldn't be abused."

Ken Clarke, Conservative MP, November 2014

The free movement of workers is a fundamental principle of the single market allowing EU Member State nationals to work and reside in EU Member States. The principle also applies generally to EEA Member States, namely Iceland, Liechtenstein and Norway. If the UK were to follow the Norwegian model, the free movement of workers is therefore very likely to continue to apply. If the UK were to follow the Swiss model, under which it would not be a member of the EU or the EEA, it could nonetheless sign up to free movement of workers through the conclusion of bilateral treaties, and it is likely that it would have to do so if it wanted to enjoy full access to the single market. Under a total exit model, whether the UK participates in the free movement of workers would depend upon the exit agreement negotiated with the EU. It is extremely unlikely that the UK would be granted access to the single market with the free movement of goods, services and capital, without the accompanying free movement of persons.

"In return for full access to the EU's free-trade Single Market in key UK industries, we would have to accept the free movement of people."

HM Government briefing paper, March 2016[20]

In an employment context, a departure from the free movement of workers would mean that EU citizens would lose the right to work in the UK and UK citizens would equally lose the right to work in EU Member States. It is likely, however, that transitional provisions would be put in place, so the changes to workers' status would occur over time. If the UK was no longer required to respect this principle, both UK and EU employers would likely face administrative burdens associated with visas for their workers and costs

[20] 'Alternatives to membership: possible models for the United Kingdom outside the European Union'.

[19] Directive 2003/41/EC, 3 June 2003 on the activities and supervision of the institutions for occupational retirement provision, OJL 235, 25/09/2003.

associated with complying with any new arrangements. The loss of free movement of workers should therefore be of significant concern to UK and EU employers.

How would Brexit affect individuals' pensions?

Much of EU pension legislation has already been incorporated into the UK pension regulatory framework. Therefore Brexit would be unlikely to produce any immediate change to the UK pension landscape, and to the pensions of UK nationals residing in the UK.

The position may be different for UK nationals working in other EU Member States. In relation to National Insurance, UK nationals working for an employer in an EEA Member State or in Switzerland will ordinarily pay social security contributions in that country rather than National Insurance contributions. Accordingly, they may be eligible for benefits from that country.

However, while UK citizens residing in EEA countries, Gibraltar and Switzerland are currently entitled to state pension increases[21], Brexit may result in such automatic entitlement no longer being available. As a result, UK citizens working in countries that do not have a bilateral agreement with the UK may be subjected to a freeze in pension increases. The extent to which there will be any other changes to the pensions of UK nationals living abroad is unclear.

[21] https://www.gov.uk/government/publications/state-pensions-annual-increases-if-you-live-abroad/countries-where-we-pay-an-annual-increase-in-the-state-pension.

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7. Intellectual property

It is likely that Brexit will affect IP owners in terms of the actual rights they hold and how they can exploit and enforce them in the future. Businesses should start considering possible strategies for the filing, management and enforcement of their IP rights and review whether their licensing arrangements need "Brexit-proofing"

Enforcement

Rights

National	Pan-European
UK Patents	Community Trademarks (CTMs)
UK Trademarks	Community Design Rights (CDRs)
UK Design Rights	Unitary Patents (UPs)

Licensing

National rights

National rights should remain largely unaffected in the short term by Brexit. The UK Intellectual Property Office will continue to grant national patents, trademarks and design rights as it currently does.

It is likely that UK statutes underpinned by EU legislation (such as the Trade Mark Directive[22]) will remain unchanged for the time being. However, the UK Parliament would in future be free to introduce new or amended legislation and would no longer be subject to the rulings of the Court of Justice of the European Union. It is possible that the UK interpretation of this legislation will diverge from the rest of the EU relatively quickly.

European patent law largely derives from the European Patent Convention, which is an international agreement separate from the EU that should be unaffected by Brexit. Upon grant, the European Patent ("EP") becomes a bundle of rights that are managed and enforced on a national basis, and so any EPs validated in the UK will continue to be valid. It is unclear how the UK Government will deal with other EU legislation surrounding patents; for example, the supplementary protection certificates allowing extension of patent term for medical and plant products.

Pan-European rights

Unlike EPs, Community Trade Marks ("CTMs" – soon to be called "EU Trade Marks") and Community Design Rights ("CDRs") are single pan-European rights automatically valid in all EU Member States. It is uncertain what will happen to these rights following Brexit. It is possible that they will be split into a UK trademark

[22] Directive 2008/95/EC of 22 October 2008 to approximate the laws of the Member States relating to trademarks.

or design right and a CTM/CDR valid in the rest of the EU. Alternatively, the UK Government may legislate to allow all existing CTMs and CDRs to continue to apply in the UK without the need for a separate UK registration, but impose a requirement for separate registration for all new rights in the future. Of course, applying for and maintaining multiple registrations will result in additional administrative and financial burden on rights holders.

Similarly, the Unified Patent ("UP") will be a single pan-European right valid in all contracting states. The UP will enter into force upon the ratification of the Unified Patent Court ("UPC"), the complementary new litigation system, which is expected to occur in the first half of 2017. The preparations for the introduction of the UPC both at European and at national level are at an advanced stage with the UK currently committed to implementing the new regime. In the event of Brexit, however, it would be difficult for the UK to maintain this position and it is likely that the UPC Agreement would require renegotiation and amendment to proceed without the UK. There would also be issues such as the location of the London section of the Central Division to resolve. This creates considerable uncertainty for prospective applicants of UPs and the holders of EPs to which the same regime will apply automatically (unless an opt-out is exercised).

Licensing

If the UK votes to leave the EU, businesses will need to review their IP licences. Changes may be required to defined terms, the territory to which the licence applies and the actual rights licensed[23]. This may open the possibility for renegotiation of the rest of the terms, so both licensees and licensors will need to think strategically about the most advantageous time to raise the issue. Agreements may need some "Brexit-proofing". The effect of Brexit on contracts and the potential for disputes is also considered in the Dispute Resolution section of this briefing.

Enforcement

In the event of Brexit, it is likely that pan-European remedies, such as cross-border injunctions, would no longer cover the UK and may require a separate application to the UK courts. Similarly, some of the remedies and defences that were "imported" from EU legislation (such as the exhaustion of rights) may no longer be available depending on the post-Brexit model adopted.

[23] For example, licences may refer to defined CTMs/CDRs and to the EU as the licensed territory with no provision for a post-Brexit landscape.

IP rights	Issues to consider on Brexit	Strategies
UK national rights	Changes to legislation applying to national and pan-European rights	Careful monitoring and analysis of both UK and EU-wide legislation and case law
Community Trade Marks Community Design Rights	Uncertainty regarding UK's treatment of pan-European rights Increase in cost and administrative burden of maintaining these rights Uncertainty regarding enforcement	Consider if a separate UK national or an international right should be applied for Consider and estimate the implications for the portfolio Consider if separate application to UK court may be necessary for enforcement of rights
European Patents Unitary Patents	Uncertainty regarding implementation of the Unified Patent Court ("UPC") Agreement Uncertainty regarding enforcement	Consider opting out of the UPC for existing EPs. For future patent protection apply for national patents or traditional EPs (opted-out of the UPC) until more certainty
IP licensing	IP licences may not cover UK when outside the EU Brexit issues may trigger renegotiation of terms of existing licences	Review existing licensing arrangement and identify any prospective issues

8. Environment and climate change

EU membership has been widely regarded to have had a positive effect in the UK in terms of environment and climate change law: the environmental sector has raised concerns about the "rolling back of environmental regulation" should the UK leave the EU

The status of environmental and climate change law

EU legislation governs most of the UK's environmental and climate change law and policy and so Brexit is likely to have significant and direct implications for these areas. The key reasons for the high level of entwinement of UK and EU law in respect of environmental matters are that:

- environmental and climate change law and policy address issues that transcend the borders of EU Member States, such as pollution and carbon emissions, and so there is a strong argument for cross-border rather than national action;

- international agreements such as the Kyoto Protocol are a key feature of environmental law and the EU's institutions are used to negotiate and implement such agreements on behalf of and within the EU; and

- common environmental standards are required for the efficient functioning of the single market.

Environmental and climate change law is also an area where most commentators consider that EU membership has had a positive effect on the UK, which was previously labelled the *"dirty man of Europe"*. When the UK Government published its 'balance of competences' review of EU environmental and climate change policy in February 2014, it reported on a *"broad consensus among all sectors [of UK business] that EU action is needed on environment and climate change matters"*[24]. There is a general recognition that membership of the EU has been particularly positive in respect of imposing targets on waste and climate change and the measures taken relating to air and water quality. The existence of a union with environmentally aware countries such as Germany, Sweden and Finland is also recognised as having helped to accelerate UK action on environmental matters. Against this background, the environmental sector has raised concerns about the *"rolling back of environmental regulation"* should the UK leave the EU[25].

As with all areas of law, the effect of Brexit will depend on which model is adopted for the UK's post-Brexit relationship with the EU; which of the UK's current laws will be retained; and what approach is taken in respect of the status of EU law and transitional arrangements.

[24] HM Government, '*Review of the Balance of Competences between the United Kingdom and the European Union Environment and Climate Change*', February 2014, page 9.
[25] Matthew Farrow, director of the Environmental Industries Commission, 19 November 2015.

The key points of comparison between the different models from an environmental and climate change perspective are:

The Norwegian model	• The UK would be bound by the EEA Agreement, which incorporates key EU environmental directives (including in respect of environmental protection, water, air, waste and noise) and the Registration, Evaluation, Authorisation and Restriction of Chemicals (REACH) regulation. However, the Wild Birds, Habitats and Bathing Water directives are not incorporated. • The directives regarding the EU Emissions Trading Scheme (a cap and trade system that sets a decreasing cap on the total amount of certain greenhouse gases that can be emitted by factories, power plants and other installations) also apply to EEA countries.
Either the Swiss model or total exit	• The UK would not be bound by the environmental obligations provided under EU law or the EEA Agreement. • The UK would continue to be bound by any international agreements to which it is party or to which it would become a separate party post-Brexit. • The UK could become a member of the European Environment Agency, an agency of the EU that has the objective of providing sound, independent information on the environment. Membership is not limited to EU Member States: Switzerland and Turkey are members. • The UK would not be bound by the requirements of REACH. However, to ensure that it has access to the EU market, it is most likely that the UK would implement similar chemicals legislation. The same rationale would apply to other similar EU environmental and health and safety requirements in respect of products sold in the EU. • UK energy-intensive installations would not be required to participate in the EU Emissions Trading Scheme. However, it is to be expected that the UK would maintain a similar system at national level. There may also be opportunities for the UK to link its scheme with that of the EU to benefit from a larger and more liquid European market for the trade of carbon allowances. Switzerland and the EU have recently announced an agreement on such a linkage after five years of talks.

The effect on current EU law and transitional arrangements

Most EU environmental law takes the form of directives, so the UK will need to consider whether it wishes to retain the national law that has implemented them. The UK seems likely to retain climate change and waste targets, but there will be certain areas where the UK Government will be encouraged to repeal or add “flexibility” to measures that are considered to place unnecessary restrictions on development and economic growth. For example, developers, including those in the renewables sector, have criticised the restrictions that can be placed on development by the requirements of the Wild Birds and Habitats directives. However, such demands will need to be balanced against the UK's long heritage in this area of protection and the calls for more action to address the decline in habitats and species.

From an implementation and enforcement perspective, there are four key issues that the UK Government and the regulators will need to consider:

i. A significant body of environmental regulations, such as the Environmental Permitting Regulations, refer to concepts and definitions in EU directives. Environmental lawyers have raised concerns about how the national law would be interpreted if there are limitations on being able to refer to EU law or materials following a Brexit.

ii. The extent to which EU case law can be used by the UK national courts, particularly as the European courts have been asked to interpret points of law on a wide range of environmental topics.

iii. There are many environmental concepts within the EU, such as "Special Areas of Conservation", that will need to be introduced into national law if the same framework of environmental protection is to be adopted post-Brexit.

iv. Depending on the outcome of the referendum and the approach taken to transitional arrangements, there may be impacts on new measures under EU law that have been introduced as directives and are required to be implemented during the exit negotiations. An example of this is the Environmental Impact Directive, which is to be implemented into national law by 16 May 2017. There will be uncertainty regarding the approach to be taken, which will have consequences for large developments and projects.

The theme of uncertainty is central to commentary on the subject of environmental and climate change law in the context of Brexit discussions.

> *"The environmental rules of engagement with the EU after Brexit are very uncertain and would be subject to lengthy and protracted negotiation due to our new status as an outsider. We would no longer be able to shape EU policy and our influence on the environmental performance of other member states would decline very sharply once we were no longer at the negotiating table."*
>
> **Letter to the Secretary of State for Environment, Food and Rural Affairs dated 27 January 2016, from a group of signatories including four former chairs of UK environment agencies**

9. Real estate

Land law in the UK would be almost entirely unaffected by Brexit, but opinion is split on the commercial effects

In stark contrast with environmental and climate change law, land law in the UK (or rather the three separate systems of land law within it) has remained almost entirely unaffected by the UK's membership of the EU. Brexit, in any of its possible forms, is therefore unlikely to have any direct legal implications for the way in which UK land is held and dealt with.

The likely effect of a vote to leave the EU on the property industry more generally is less clear. In the short term, there would be an inevitable period of uncertainty while terms for the UK's future relationship with the EU were settled. In the longer term, there are fears of reduced demand, including for office space, if multinationals relocate from London. But some doubt that leaving the EU would ultimately result in any decrease in the UK property market's attraction for foreign capital.

The Alternative Investment Fund Managers Directive ("AIFMD") is one of very few examples of direct EU involvement in the property industry. AIFMD provides a regulatory framework for alternative investment fund managers, including managers of real estate funds[26]. Importantly, that includes a passport allowing the marketing of such funds throughout the EU. The loss of that passport could restrict access to capital from the EU, but again much would depend on the model for post-Brexit relations with the EU.

[26] AIFMD and other similar legislation is discussed in more detail in the Financials services and insurance section of this briefing.

10. Tax

The immediate effect of Brexit on UK tax law would likely be minimal, but over time the UK may make changes to VAT and duties, and if it did not join the EEA it would no longer be subject to the State aid rules (including in relation to tax)

The immediate effect of any form of Brexit on UK tax is likely to be minimal. Almost all EU tax-related changes have been enacted into UK legislation or reflected in UK case law developments or established HMRC practice.

Over time, changes could be made to VAT and duties, but anything more than minor tinkering seems unlikely. In the sphere of groups of companies, changes to transfer pricing and group relief (among others) have been enacted following decisions of the ECJ, and would likely remain if the UK followed the Norwegian model and left the EU but joined the EEA, as would exemptions from withholding tax (“WHT”) on interest and royalties. The UK’s extensive network of double-taxation conventions would be unaffected by Brexit.

VAT and duties

VAT is generally applied only within the EU, and so any form of Brexit would give the UK freedom to amend VAT or abolish it entirely. Given that VAT is so well established within the UK tax regime, its replacement by another goods and services tax seems inconceivable - it has also accounted for just over 20% of all UK tax receipts on average over the last five years, an amount of just under £500 billion in that period[27]. More likely is that the UK would use the freedom from EU constraints to correct some of the perceived injustices and oddities of the VAT system.

The EU also mandates minimum levels of duty for alcohol, tobacco and energy. Given that the UK levels are currently far above the EU minimum levels, any impact on these duties if the UK voted to leave the EU is unlikely.

The UK, on leaving the EU, would also leave the customs union. There would therefore be customs procedures imposed on exports between the UK and the EU. If the UK left the EU and did not join the EEA, then absent any bilateral free trade agreements, customs duties and VAT on imports may be imposed.

The Norwegian model

If the UK left the EU but joined the EEA, the immediate effect would be that EU directives such as the Mergers Directive, Parent-Subsidiary Directive and Interest and Royalties Directive would no longer apply to the UK. These directives, among other things, prevent the imposition of WHT on dividends, interest and royalties in particular circumstances.

[27] HM Revenue and Customs: ‘HMRC Tax and NIC Receipts, monthly and annual historical record’, 19 February 2016

While the directives would no longer apply, under the Norwegian model the effect of this would be minimal. The UK does not currently impose any WHT on dividends (even when paid to non-EU persons) and so is unlikely to introduce WHT in such cases. Moreover, while the UK does impose WHT on interest and royalties paid to certain non-EU persons, any attempt to extend these to EU persons would likely contravene the principles of freedom of establishment or free movement of capital – both of which would continue to apply within the EEA. The same would be true for payments received in the UK from EU persons.

The continuation of these two freedoms in particular would also mean that many of the changes to UK tax rules that have resulted from decisions of the ECJ would have to remain. Changes to the group and consortium relief rules, extension of the transfer pricing rules to wholly domestic transactions, and exemptions from the transfer of assets abroad and controlled foreign company rules have all resulted from these freedoms, and so could not be removed were the UK to join the EEA.

In addition, the 2012 first-tier tribunal decision in *HSBC Holdings PLC and The Bank of New York Mellon Corporation v HMRC* has confirmed that, while the 1.5% SDRT charge on issues into depositary receipt and clearance systems is contrary to the EU Capital Duties Directive, the charge is also contrary to the free movement of capital. Such an SDRT charge would therefore remain unlawful were the UK to join the EEA after leaving the EU.

State aid rules, while more typically seen as part of competition law, have been recently deployed in a significant way against EU Member States seen to be providing “sweetheart” deals to tax-payers. These rules would continue to apply were the UK to join the EEA, and so the restriction on granting State aid (whether through the tax system or otherwise) would remain.

The Common Consolidated Corporate Tax Base (“CCCTB”), recently re-launched by the European Commission in a further attempt at harmonisation of corporate taxation, remains strongly opposed by the UK. If implemented, it would be very unlikely to extend beyond the EU Member States (i.e. it would not extend to the EEA). Brexit, however, makes the CCCTB far more likely to come into effect within the EU as the UK (along with Ireland) is one of the key opponents and, as a proposal on tax, the CCCTB requires unanimity among the 28 Member States. Removing the UK from the opposition list could well leave countries such as Ireland looking increasingly isolated.

> *“The CCCTB has been around a very long time. It is a proposal still looking for a justification.”*
>
> **David Gauke, Financial Secretary to the Treasury, 1 June 2015**

Also more likely to proceed is the Commission’s recently proposed Anti-Tax Avoidance Directive. While again this is limited to the EU Member States and would not apply to the EEA, approval is more likely without UK influence in the EU decision-making process.

> *“We will not stop cross-border tax avoidance with 28 national responses.”*
>
> **Pierre Moscovici, European Commission Tax Commissioner, 28 January 2016**

On a similar theme, the UK would be excluded from automatic exchange of information within the EU, although given the implementation of the OECD's Common Reporting Standard in 2017, most of the same information would continue to be exchanged.

The Swiss model

The Swiss model entails a particularly unique approach, recognising the "special case" of Switzerland, which has access to the single market only in particular areas. There is free movement of workers, but there is no free movement of capital, and freedom of establishment is very restricted. There are prohibitions on State aid in the bilateral agreements between Switzerland and the EU; however, there is significant disagreement between Switzerland and the EU on the extent to which these apply[28]. It is worth noting that even where Switzerland has similar freedoms or rules to those in the EU treaties, the same interpretations cannot be applied.

While the terms of such a relationship would need to be negotiated, it is likely that, as with a total exit model, the UK would be able to impose WHT on interest and royalties paid to EU persons and EU persons would also be able to impose WHT, and to roll back those changes required by the ECJ (including the 1.5% SDRT charge at issue in HSBC Holdings). The UK's extensive network of double-tax conventions, and the WHT rates contained within them would, however, continue to apply.

Under the Swiss model, the UK would gain complete freedom in relation to VAT and duties.

Total exit

If the UK left the EU and did not join the EEA or form some kind of special relationship as Switzerland has done, the UK tax position would largely mirror that under the Swiss model. The UK would recover complete freedom in relation to tax and the provision of State aid.

[28] The impact of Brexit on State aid law more generally is discussed in further detail in the Competition law and State aid section of this briefing.

11. Infrastructure, energy and natural resources

For IEN, the big picture is one of continuity, but the Brexit debate has introduced uncertainties that may delay policy formation and investment for years

If the UK votes to leave the EU, the contours of the country's infrastructure, energy and natural resources ("IEN") sectors are not expected to shift overnight. While the sound and fury attending a renegotiation of the UK's trade relationship with its European neighbours is not likely to drive away the policy fog that has pervaded IEN in recent years, there are good reasons to believe that the eventual outcome would be characterised by continuity, not triumph or disaster.

A well-managed Brexit may present the UK with an opportunity to renew its vision for a public infrastructure fit for the twenty-first century, with global investment matched to projects without potentially distorting constraints imposed by the EU. The pessimist's rejoinder, however, would be that this sanguinity is misplaced, that the UK is running the risk of throwing away the benefits of market integration out of sheer bloody-mindedness, only to find that it commands less control over its infrastructure and energy policy than before.

Reasons to be cheerful

In the IEN sphere, Brexit could allow the UK to forge its own path with regard to procurement, subsidy controls and oil and gas.

A post-Brexit UK could relax its procurement regime by streamlining the process for lower value contracts and allowing high-priority projects to be treated differently where appropriate. Although the net effect of such reforms is difficult to assess, it seems likely that the removal of obstacles to public investment would tend to reduce transaction costs and accelerate the implementation of complex projects. If the UK left the EU but did not join the EEA, it would not be subject to the EU rules prohibiting anticompetitive State aid (as discussed in the Competition law section of this briefing). Removing the requirement for European Commission approval of State aid could ease project timetables and reduce execution risk for investors participating in complex public-private ventures. UK Government authorities could foster productivity-increasing growth by trialling new approaches to using State resources to allocate resources to essential infrastructure and networks and reduce capital costs. At the same time, there is a risk that, rather than nurturing a flowering of investment in critical projects, the slackening of such important controls would merely lead to waste and cronyism on a monumental scale.

A different risk calculation applies to the oil and gas sector, where there may be scope to reduce the regulatory burden on North Sea operators by repealing EU directives that increase costs to producers, such as the prescriptive offshore safety directive imposed on the sector in the wake of the Deepwater Horizon accident and the threatened moratorium on deep-water drilling. Onshore, the UK may find it easier to experiment with unconventional gas, reducing import dependency and increasing the contribution of relatively clean natural gas to the UK's energy mix.

There is no guarantee that such steps would be feasible politically, however, not least because resistance to, for example, airport expansion and fracking tends to be domestic in scope rather than reflecting any pressure from the EU. Withdrawal from the EU would not necessarily derail the transition to a low-carbon economy, however, since the most significant climate change targets are enshrined in UK statute and in some cases go further than EU requirements. There is no question that the UK will continue to have to find multilateral solutions to cross-border environmental challenges. Participation in EU structures such as the Emissions Trading Scheme has been extended to EEA States such as Norway and Iceland in recent years, so the UK may continue to participate in these structures if it leaves the EU but joins the EEA.

Regulation without representation: the worst of all worlds?

UK interests in oil, gas and natural resources will remain a global concern while London remains an attractive forum for raising capital. Local infrastructure and energy needs, however, will remain subject to geographical constraints. In this light, regional integration will generally offer the greatest potential for affordable expansion, consumer welfare and productivity gains. While the merits of market regulation have been contested by those who resist the meddling of the pantomime villain *"bureaucrat in Brussels"*, the policy goals championed by the European Commission – cross-border compatibility, a preference for competitive markets to governments picking winners and a resistance to protectionism and discrimination – are broadly supported across the range of opinion.

Nor is it self-evident that other models for trade with Europe, such as the Norwegian model and the Swiss model, offer a genuine alternative to the status quo. As discussed in the second edition of this briefing, the UK runs the risk of cleaving to a policy framework fashioned in Brussels without having a say in how it is fashioned. UK companies and consumers cannot be assured that such passive obedience to an external agenda will deliver a good deal. This would be a problem in even the most economically favourable conditions, but it is particularly acute at a time when the UK needs regulatory stability to encourage investment to build, replace and refresh its railways, runways, tunnels, ports, bridges, broadband and power stations.

Energy and infrastructure policy has traditionally been the preserve of individual Member States. It is only in recent decades, culminating in the inclusion of energy and transport as shared competences of the EU in the Lisbon Treaty, that the prospect of a meaningful single market has become feasible in this space. To this end, the UK has played a crucial leadership role in agitating for the removal of trade barriers and the opening up of erstwhile monopoly sectors. The UK has usually practised what it preached, for example by pioneering the liberalisation of the electricity and water markets, embracing external investment in national infrastructure, and inviting European firms to tender for services historically provided by the public sector or national champions.

The irony is that the benefits of the market competition and transparency in the IEN sectors cultivated by the European Commission may only be realised in the coming decades, with the UK at risk of leaving before the party has begun. Depending on the post-Brexit settlement that emerges, regulatory obstacles may prevent UK companies from competing on a level playing field with European companies, which the UK Government may be powerless to resist without formal access to EU institutions. Where once the future promised free access to a dynamic market of 500 million consumers, the terms of any post-Brexit trade agreement with European neighbours are likely to be marred by hostility, mistrust and the perceived need to deter other EU Member States from following the UK's lead. Co-operation and competition may well be jettisoned for protectionism and turf wars.

In respect of the energy sector, the UK Government has argued that the historic challenges posed by the "trilemma" of delivering a reliable supply of affordable energy from low carbon sources is best mitigated through co-operation with European neighbours. The recent moves to integrate European power and gas markets into a cross-border "energy union" have increased market liquidity and, crucially, the supply of baseload electricity to UK homes and businesses at a time of falling capacity margins and increasing intermittency on the grid. It is unclear whether, for example, the roll out of interconnectors with France and the Netherlands would continue if EU targets ceased to apply in the UK, and cross-border capacity market auctions may be suspended while replacement trade agreements can be negotiated.

Despite these risks, the bulk of the costs of leaving the EU, at least in the IEN context, may only be felt at the margins. Ignoring the uncertainties, the big picture is one of continuity. Leaving the EU would not be likely to affect electricity and gas market regulation, for example, and membership of cross-European regulatory bodies such as CEER, ENTSO-E and ENTSO-G is not restricted to EU Member States. The UK Government could elect, like Switzerland, to make use of EU market architecture such as the REMIT regime, instead of drawing up its own rules from scratch. Even in a post-Brexit environment, the UK Government is unlikely to take deliberate steps to disconnect from networks shared with European neighbours. That being said, there is little doubt that the Brexit debate has introduced uncertainties that may delay policy formation and investment for years, while the potential prize offers a dubious sovereignty at best.

"Given the multinational nature of energy markets and companies, even withdrawal from EU would probably not affect the direction of travel."

"Leaving the EU", Research Paper 13/42 House of Commons Library, July 2013

12. Financial services and insurance

Rather than resulting in a "bonfire of red tape", at least in the short to medium term, considerably more uncertainty and complexity in regulation of financial sector firms operating from the UK is expected. The compliance burden for some UK firms may increase

The UK has the largest financial services sector of any EU Member State and this sector would be greatly affected by a decision to leave the EU. This is because the great majority of financial services regulation in the UK derives from EU law and international standards made by bodies such as the Basel Committee on Banking Supervision ("Basel Committee") and the Financial Stability Board ("FSB") are implemented in the UK through EU law.

However, the regulatory landscape has changed fundamentally since the financial crisis, with increasingly prescriptive regulation for banks, investment funds, insurers, rating agencies and other financial services providers and markets globally. Brexit would therefore be most unlikely to result in a "bonfire of red tape" in the financial services sector. The UK would remain bound by international standards adopted by international fora such as the G20, the FSB, the Basel Committee, IOSCO and the International Association of Insurance Supervisors ("IAIS"), and as a member of these bodies it would continue to have influence (and perhaps more influence outside the EU as the UK would no longer be constrained by EU solidarity) over those standards.

"You wouldn't immediately assume that there is a golden world out there where it's all different."

Andrew Bailey, Bank of England Deputy Governor, 3 February 2016

Against that, there is the question of UK access to the single market. Under the Norwegian model, the UK would be bound by existing and future EU directives and regulations in financial services as a condition of maintaining single market access, but without any voting rights on the resulting legislation. Under the Swiss model, there is potentially more flexibility, although greater uncertainty as there would need to be separate agreement on all future legislative changes if the UK wished to retain access to the single market. Under a total exit model, unless the UK were able to negotiate a free trade agreement offering access to (parts of) the single market, it would be treated as a 'third country' and would carry on financial services business in the EU on no more favourable terms than any other country. Under a total exit model firms will not, as a general matter, enjoy a European 'passport' to establish a branch or provide services on a cross-border basis and will need to obtain local authorisation consistent with EU minimum standards for cross-border operations. Alternatively, UK firms may decide to establish an EU/EEA subsidiary to carry on EU business. In addition, in the longer term being outside the EU may expose UK firms to more potential sources of financial regulation than is the case at present.

As a result of EU exit, the City of London may come to be seen as a less attractive place to do business within the European time zone, with consequences for employment and tax revenues from business generated by the financial sector. While this outcome would ultimately depend on the terms that the UK negotiates for access to the EU single market, if any, this access is very likely to require the UK to reach some 'equivalence' standard with respect to EU financial sector legislation. 'Equivalence' for these purposes is likely to be determined by the European Commission and to involve a significant element of discretion.

The reform package agreed upon by the 28 EU Member States in February 2016, to be implemented should the UK vote to remain in the EU, includes various measures on economic governance that address the position of the financial services sector (discussed in the third edition of this briefing series), including a prohibition on discrimination against the use of non-Euro currencies and a right for the UK to oppose the adoption by qualified majority of legislative acts in the area of economic governance (intended to stop the eurozone states from "caucusing" against the non-eurozone). These measures would not be implemented if the UK were to leave the EU.

If the UK votes to the leave the EU, the process for withdrawal is unlikely to be expeditious, and if there is a failure to agree on the future relationship of the UK with the EU the Treaties would only cease to operate after the lapse of two years[29]. Depending on the terms of Brexit, the UK's resulting relationship with the EU could create operational and legal barriers for financial services firms that do not currently exist, which could lead to a greater propensity for financial services firms to expand their offering through other financial centres in Europe to the detriment of the UK.

The effect of Brexit on the financial services industry will depend on the model that is adopted for the UK's renegotiated relationship with the EU.

The Norwegian model

If the UK were to leave the EU but join the EEA and EFTA, this would likely result in the least disruption to financial services providers, as the UK would continue to have access to the EU single market under the EEA Agreement. The main difference is that the basis of the UK's participation in the single market would flow from the EEA Agreement and not the EU Treaties.

When the EEA Agreement was signed in 1992 all the existing EU law relevant to the single market was adopted as part of the annexes to the Agreement. Thereafter, as new EU legislation is adopted the EEA is expected to adopt it through modifications to the annexes. In theory, the adoption of new legislation is not automatic, although in practice this has been the case. Again, in theory, an EEA State can negotiate derogations from the relevant new EU legislation, although these are rarely granted. The result is that current and new EU legislation in the field of financial services would continue to apply to UK banks, investment firms, insurers and other financial services providers, once it has been incorporated into the EEA Agreement.

However, access for EEA States to the single market for financial services is at present not complete, because the EEA is making slow progress in incorporating EU legislation on financial services into the EEA Agreement. As a result of the differences in regulation, access in some parts of the financial services sector is presently limited. For example, the Bank Recovery and Resolution Directive has not yet been adopted into the EEA Agreement.

[29] The Treaties would cease to apply to the UK from the date of entry into force of the withdrawal agreement or, failing that, two years after the UK submits its notification of intention to withdraw, unless the European Council (comprising the 27 remaining Member States), in agreement with the UK, unanimously decides to extend this period.

Moreover, the UK's right to be involved in the decision-making process on new EU legislation would therefore be limited to a consultation right: the UK would have no right to vote on the decisions taken in the Council of Ministers and there would obviously be no UK members of the European Parliament.

It follows that the EU legislation on the prudential supervision of banks (CRD IV and CRR), investment firms (MiFID II and MiFIR) and insurers (Solvency II and the related Commission Implementing Regulation) would continue to apply, although the UK would have no direct influence on any future proposals to amend that legislation. The same would apply to the cap on bankers' bonuses, the Alternative Investment Fund Managers' Directive ("AIFMD") and the European Market Infrastructure Regulation ("EMIR"). UK authorised banks, investment firms, insurers and payment institutions would therefore continue to be free to establish a branch in EU Member States and to provide services on a cross-border basis from the UK or from an EU branch. Life, in other words, would go on much as it does now for the financial services sector, except that the UK would not have a say in how the rules that affected the financial services market were set.

The Swiss model

If the UK were to follow the Swiss model and negotiate access to the single market through a series of bilateral agreements, it is unclear what access and under what conditions UK financial services firms would be able to provide services or establish branches in EU Member States. The resulting uncertainty could be expected to have a negative effect on the financial services sector, whatever the ultimate outcome of the negotiations.

In any event, it is highly unlikely that the UK would be able to benefit from access to the single market in financial services without adopting equivalent regulations: the UK would therefore not be able to adopt a materially lighter regulatory burden on financial services firms than that required by the EU, or a heavier one on incoming EU firms, although the UK would, in principle, be free to impose more onerous obligations on UK-authorised firms. For example, Switzerland has adopted legislation equivalent to CRD IV and CRR for banks and Solvency II for insurers, albeit with modifications. In some cases, this has resulted in heavier regulation of certain financial groups than would be the case in the EU, as Swiss regulators have also sought to apply their own 'gold-plating' to the EU rules.

The Swiss model would give the UK even less influence over future EU legislation – directly affecting UK financial services firms – as it would likely be presented on a 'take it or leave it' basis if the UK wanted to continue to benefit from access to the single market. Given the need to amend bilateral agreements, there is a greater risk of delays in the process of agreeing amendments and consequently of UK law being 'out of sync' with applicable EU law – thereby stalling market access for UK firms. This could make the UK process for enacting financial services legislation considerably more complex and time consuming than it is today.

It is to be expected that existing and future EU financial services legislation would in practice continue to apply to the UK under the Swiss model. The UK courts would not be bound by decisions of the ECJ or the EFTA Court, and would not be able to refer to either court to determine the meaning of the relevant legislation. However, where a bilateral agreement incorporates the substance of an EU regulation or directive then the UK courts would be entitled to have regard to decisions of the ECJ and EFTA Court.

Total exit from the EU

If the UK exited the EU and did not negotiate a new free trade agreement, its trade with the EU would be based on WTO principles.

It should be noted that the majority of financial services legislation in the UK currently derives from EU directives and regulations. It would therefore not be possible simply to repeal the European Communities Act 1972, as such a step would leave large areas unregulated. In the interim, it could therefore ironically be necessary for the UK Government, following a total exit, to pass legislation re-enacting relevant EU legislation. It is possible that the period of negotiations surrounding exit would allow sufficient time to decide which pieces of EU legislation to retain, which to amend and which to abrogate completely. This is, however, unlikely given the volume and complexity of that legislation and the potentially conflicting objectives of retaining access to the single market and meeting the inevitable demands from some quarters not to re-enact certain aspects of EU legislation.

International standards would continue to apply

The main benefit of total exit to the UK would be that the UK could design its own system of financial regulation, based on its own assessment of the appropriate trade-off between the benefits of regulation and consumer protection versus the costs of stifling innovation and placing burdens on the financial services sector.

A significant caveat to this is that the UK is a member (and would in all probability continue to be a member) of international standard-setting bodies such as the Basel Committee and the FSB, and would remain bound to apply the standards of those bodies. The current prudential requirements for banks would therefore continue to apply to UK banks subject to three caveats:

- where the Basel Accord is more liberal than the EU rules (e.g. in the area of remuneration) the UK could follow the Basel approach; but
- as the Basel Accord sets only minimum standards, the UK could still choose to impose higher standards on UK authorised firms; and
- the UK could restrict the application of the Basel rules to internationally active banks and apply a lighter regime to small banks.

The second point could be a particular concern for UK-domiciled banking groups, as the UK would be freed from maximum harmonisation and the EU single rule book, and would be free to take additional measures to prevent another banking sector crisis in the UK. Historically, UK regulators have, where permitted by EU regulation, often imposed more stringent standards on UK financial services firms than required by EU law. This tendency to ‘gold plate’ EU law has been held in check by the concept of ‘maximum harmonisation’ that applies in some EU legislation, including most of the CRR, the Solvency II Directive and implementing regulation and MiFID II. Freed from these constraints in a Brexit scenario, it is possible that UK regulators would gradually revert to type and only political intervention might stifle over-zealous UK regulatory activism.

In the case of insurance, there is less international agreement as to the appropriate prudential standards, although the IAIS has published international minimum standards with which the UK would be expected to comply. These are significantly less detailed than the prudential rules that apply to banks and (subject to what is said below) would offer the UK scope to adopt a different and significantly less prescriptive regime for insurers than Solvency II.

In terms of Over the Counter ("OTC") derivatives, the UK would need to follow the G20/FSB standards on central clearing of derivatives and the margining of non-centrally cleared derivatives. In terms of hedge funds, there are no generally agreed standards and the UK would be free to legislate or not. The treatment of credit rating agencies is particularly unclear although the UK would be expected to comply with G20 requirements on oversight presupposing some regulation. There would also remain the question of access by UK Central Counterparties ("CCPs") to the EU, which is currently guaranteed under the EMIR Regulation. Under a total exit model, UK CCPs would be treated in a manner analogous to US CCPs.

Subject to compliance with internationally agreed standards, the main constraint for the UK in adopting different rules to those applicable in the EU is whether the UK would wish to meet the standard of 'equivalence' in EU financial services legislation that will continue to govern access to the single market. This will potentially have significant consequences for firms based in the UK.

Banks

The CRD IV Directive requires that *"the rules governing branches of credit institutions having their head office in a third country should be analogous in all Member States"* and stresses the importance of providing that these rules are not more favourable than the rules that apply to branches of credit institutions from another Member State. In other words, non-EU banks should not be treated more favourably than EU banks. The EU is able to conclude agreements with third countries providing for the application of rules that accord such branches the same treatment throughout the EU. Branches of banks authorised outside the EU do not enjoy the freedom to provide services or the freedom of establishment in EU Member States other than those in which they have locally authorised branches.

It follows that UK banks wishing to access EU or EEA Member States with the same treatment will be subject to a requirement of equivalence. If the UK left the EU and relevant UK rules were not considered to be equivalent to CRD IV, UK firms wishing to operate in the EU/EEA would need to incorporate a subsidiary within the EU/EEA to carry on business. Moreover, even if equivalence were found then there would be no right to 'passport' from the UK to other EU jurisdictions. UK-based banks would therefore need to obtain separate authorisation in each EU/EEA jurisdiction where they sought to carry on business absent an agreement with the UK to apply provisions that accord to branches of a bank or an investment firm having its head office in the UK identical treatment throughout the territory of the EU. This agreement may not be a foregone conclusion.

If the UK left the EU then the Bank Recovery and Resolution Directive would cease to apply in the UK. There would therefore be no formal arrangement for the mutual recognition of bank resolution measures between the EU and the UK. If the UK wished to continue to be part of the system of mutual recognition, then this would need to be separately negotiated with the EU. Experience since the financial crisis of 2008-9 suggests that this would be politically very difficult and technically highly complex. The lack of an effective cross-border system of resolution in the banking sector between the UK and the EU would be a cause for concern from a financial stability perspective for both the Bank of England and the European Central Bank. In some senses it would set back the cause of cross-border resolution planning in Europe to the time before the financial crisis.

Investment firms

In terms of investment firms, under MiFID II (which is now expected to apply from 2018) a third country firm is permitted to provide investment services or perform activities directly to eligible counterparties and to those categories of clients considered to be professionals in the EU without the requirement to establish an EU branch only if the Commission has first determined that the third country's legal and supervisory regime is equivalent to that in the EU. A firm based in a third country deemed equivalent will need to apply to the European Securities and Markets Authority ("ESMA") to be included in a register of permitted third country firms, and ESMA will duly register it provided that (i) the firm is authorised to provide the relevant investment services or activities in the jurisdiction of its head office, and (ii) appropriate co-operation arrangements are in place with the relevant third country. An EU Member State may require that a UK firm establishes a branch in that State and obtains authorisation from the Member State's competent authorities to be permitted to provide services to retail clients or to those retail clients who request to be considered professionals. Establishment of a branch will be subject to local supervision and is likely to be based on a finding of equivalence.

The finding of 'equivalence' is an administrative procedure that gives considerable leeway to the Commission in making such a finding, with corresponding uncertainty before a finding has been made. There is no deadline for the Commission to reach a conclusion and there is no certainty that the UK regulatory regime would be deemed equivalent.

Under the existing MiFID there is no passport for non-EU/EEA investment firms, which must seek local authorisation to establish a branch or provide services on a cross-border basis.

Insurance

In the case of insurers under the Solvency II Directive, the Commission may make decisions that the solvency regime of specified third countries is equivalent to that laid down in Title 1 of the directive for the purpose of:

- the treatment of reinsurance contracts concluded with undertakings in that country;
- the calculation of group solvency (and, in particular, the contribution that a third country subsidiary makes to that calculation); and
- assessing prudential supervision arrangements where the parent undertaking of a group is in a third country.

The test is one of equivalence and not of identity. There are differences in the regimes that have been found to be equivalent by the Commission and Solvency II, and the UK should be free to make changes to the calculations and detailed rules under Solvency II without imperilling a finding of equivalence, although the requirements as to overall confidence level of the solvency standards would likely need to be Solvency II compliant (i.e. a 99.5% confidence level for the adoption of internal models).

There is no regime under Solvency II governing the cross-border provision of services within the EU from a branch of a non-EU insurer or reinsurer. It follows that UK insurers would need to obtain authorisation in each EU/EEA Member State in which they wished to carry on business. If the UK regime for insurance was not equivalent, then local supervisors are likely to require the establishment of a locally incorporated subsidiary.

The requirement for Part VII transfers to be recognised in other EEA States should cease to apply. This would make such transfers more complex where there is a significant non-EU/EEA element. The Gender Directive could also cease to apply, permitting the UK Government to reinstate the insurance exception in relation to gender-neutral pricing of insurance policies.

A particular question hangs over the validity of existing (re)insurance cover if the UK leaves the EU and consequently loses passporting rights. In some jurisdictions, the regulated activity of insurance or reinsurance is regarded as being carried out in the jurisdiction where the risk is situated and not being appropriately authorised is a criminal offence. Unless addressed in the exit agreement, this could render certain steps associated with the ongoing operation of a (re)insurance contract illegal. Normally, that would not impair the policyholder's right to enforce the contract but would obviously affect the (re) insurer's willingness to continue to carry the risk and may, for example, result in some (re)insurers transferring risk to locally authorised (re)insurers.

UCITS

The same loss of passporting rights applies in relation to the UCITS Directive unless addressed in the exit agreement.

AIFMD

AIFMD applies to the managers of alternative investment funds ("AIFs")(e.g. but not limited to hedge funds and private equity). The Directive sets out a 'passport' for non-EEA funds marketed to professional investors although the coming into force of this provision is dependent on ESMA issuing advice finding equivalence. So far, ESMA has recommended that no action be taken on implementation of the third country passport pending acquisition of more data. Until 2018 the AIFMD national private placement regime is a mechanism that allows alternative investment fund managers ("AIFMs") to market alternative investment funds that are not allowed to be marketed under the AIFMD domestic marketing or passporting regimes. This principally relates to the marketing of non-EEA AIFs and any AIFs managed by non-EEA AIFMs. This would allow the temporary marketing of UK AIFs or EU AIFs managed by UK AIFMs in reliance on the national private placement regime of EU/EEA Member States.

Credit rating agencies

For credit rating agencies, the UK would need to establish a bespoke legislative framework to meet G20 commitments (likely involving FCA regulation). This is likely to result in significant uncertainty for the sector. If the UK regime was deemed 'equivalent' then ratings issued by a UK credit rating agency could be endorsed for use in the EU by an EU credit rating agency. As with other Single Market legislation, there would be no 'passport' for UK ratings agencies to establish branches or provide services on a cross-border basis into the EU/EEA.

Market infrastructure

A particular issue concerns market infrastructure. Currently the majority of trading in euro-denominated bonds takes place in London. When the European Central Bank ("ECB") attempted to force the relocation of central clearing to within the eurozone the UK challenged successfully the ECB decision before the EU General Court[30]. It is understood that the Bank of England subsequently negotiated a memorandum of understanding with the ECB concerning the regulation of euro-clearing in London. It is questionable whether the ECB would still be willing to tolerate the majority of clearing in eurozone government debt to take place in a financial market outside the EU that was not subject to EU oversight. If this was the case, then such trading (and the corresponding revenues and employment associated with it) could migrate to a financial centre within the EU, such as Frankfurt or Paris.

A separate agreement?

The UK might seek to negotiate a separate arrangement for securing access to (parts of) the single market. This would approximate somewhat to the Swiss model considered above, and like it there are considerable doubts whether the remaining EU Member States would be willing to grant partial single market access absent accession to the EEA Agreement. As such an agreement would operate at the level of public international law it would need to be transposed into national law in all states that follow a dualist approach to the applicability of international law. The likelihood of identical transposition of measures that are directives (such as CRD IV, Solvency II, UCITS and the Payment Services directives) would be limited, as would identical application in practice. The Treaty between the EU and the UK would need to be amended whenever new directives or regulations were adopted within the scope of the free trade agreement raising potential timing and compatibility issues and the UK would of course have no voting rights on the relevant measures.

The relationship of UK financial services firms under a total exit model would therefore be considerably more complex than at present. Firms will not, as a general matter, enjoy a 'passport' to establish a branch or provide services on a cross-border basis and will need to obtain local authorisation consistent with EU minimum standards for cross-border operations. Alternatively, UK firms may decide to establish an EU/EEA subsidiary to carry on European business. In this case, the City of London may come to be seen as a less attractive place to do business within the European time zone, with consequences for employment and tax revenues from business generated by the sector.

'Third country' issues

The UK currently benefits from preferential trade agreements ("PTAs") made between the EU and various non-EEA States. Before 2006, few of these agreements contained detailed rules and commitments covering trade in services (including financial services). Since then, however, the EU has entered into various PTAs that contain detailed provisions relating to the cross-border provision of financial services, allowing the UK and other Member States to access financial services markets in each of the relevant non-EEA signatory States. Leaving the EU could threaten the UK's access to such markets. Though it would of course be open

[30] Case T-496/11; Judgment dated 4 March 2015.

to the UK to renegotiate each of the relevant agreements bilaterally, it would not necessarily be able to access the relevant markets on the same terms as it does now.

The EU is among a group of WTO members currently developing an initiative for the liberalisation of global services markets (including financial services) outside the WTO framework in the hope that the final agreement will be adopted multilaterally later. Leaving the EU would effectively withdraw the UK from these negotiations, as well as the EU's ongoing negotiations in relation to the proposed EU-US Transatlantic Trade and Investment Partnership ("TTIP"). The effect of this on the UK's ability to access financial services markets would arguably be more significant (if the final TTIP were to apply to financial services despite US opposition) than losing the access enabled by the PTAs referred to above. Negotiating bilateral arrangements with the US, even if available, would expose the UK to compliance with US standards that are unlikely to be the same as UK standards.

13. Restructuring and insolvency

The restructuring industry in England and Wales is flourishing, in part due to the ease with which the majority of procedures can be recognised in other relevant jurisdictions. In Europe, this is largely thanks to the Insolvency Regulation, the benefit of which may be lost in the event of Brexit. There are, however, other routes to recognition. In any event, the global drive to improve effective restructuring regimes is likely to lead to reform of restructuring and insolvency regimes at both domestic and international levels, and regardless of whether Brexit occurs

The status quo: a thriving UK R&I industry

At present, each EU Member State has its own corporate restructuring and insolvency regime, but EU law intervenes to overlay a broad framework of mutual recognition of proceedings and judgments. This is primarily found in the Insolvency Regulation[31], which applies to all EU Member States except Denmark (which has opted out). Proceedings that fall within the scope of the Insolvency Regulation are automatically recognised in other EU Member States (most insolvency proceedings are caught, and from 27 June 2017 when the recast regulation will take effect, many restructuring procedures as well).

To achieve this framework of mutual recognition, the Insolvency Regulation also imposes limits on the jurisdiction of the courts in each Member State. So-called "main" insolvency proceedings can only be opened in a Member State where a debtor has its centre of main interests ("COMI"), and once they are opened, the proceedings will be governed by the insolvency laws of that Member State (subject to certain exceptions). This means that UK-incorporated companies whose COMIs are located elsewhere are not able to commence main proceedings in the UK. Conversely, any company that has its COMI in the UK will be able to commence proceedings in the UK, and will benefit from automatic recognition across the EU. A number of companies have actually moved their COMI to the UK to take advantage of the highly regarded restructuring procedures available, particularly the pre-packaged administration sale (or "pre-pack"), and this has certainly bolstered the restructuring industry in the UK.

The UK's most popular restructuring tool, the scheme of arrangement, is however, a creature of company law and it falls outside the scope of the Insolvency Regulation. This has allowed the courts to set a lower jurisdictional threshold: in essence, any company can use a scheme as long as it has a sufficient connection with England and Wales. In recent years, this has most commonly been achieved on the basis of the inclusion of an English governing law and jurisdiction clause in the relevant finance documents, but the presence of assets and/or operations may also suffice. Without automatic recognition under the Insolvency Regulation, the courts have been satisfied that schemes have good prospects of recognition on other bases, for example, by applying principles of private international law. In some cases it has been suggested that the Brussels Regulation might apply to schemes[32]. This would be helpful as a basis for recognition within the EU, but it could also limit the court's jurisdiction to sanction schemes unless a sufficient number of creditors are located in England and Wales, or have submitted to the jurisdiction. For the time being, the courts have not needed to decide the point, and foreign companies have continued to find ever more innovative ways to access the scheme jurisdiction.

[31] Regulation (EU) 1346/2000 of 29 May 2000 on insolvency proceedings.
[32] Regulation (EU) 1215/2012 of 12 December 2012 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters (recast).

What would happen on Brexit?

There is no doubt that an international framework for recognition of insolvency proceedings and judgments saves the time, costs and uncertainty of applying for recognition in the courts in each jurisdiction where a debtor has assets or other interests. The Insolvency Regulation is not unique in providing such a framework. For example, the UNCITRAL Model Law on Cross-border Insolvencies provides another route by which restructuring and insolvency proceedings can obtain recognition in relevant jurisdictions, and schemes fall within in its scope (which has been hugely helpful in a number of major restructurings, including those with a connection to the US).

However, though the group of states that have implemented the Model Law is internationally diverse, very few are members of the EU. Therefore if the Insolvency Regulation ceased to apply to the UK as a consequence of Brexit, the UK Government would likely seek to agree an alternative framework for recognition of insolvency proceedings and judgments with individual EU Member States, or with the EU as a whole, perhaps without the jurisdictional limits that the Regulation currently imposes. It is unlikely that Brexit would lead to an abrupt change in the status quo: there would probably be a period in which such alternative arrangements could be negotiated.

As for schemes, the thorny question of the application of the Brussels Regulation would likely fall away (unless alternative arrangements were put in place) and with it would go one of the potential routes to recognition, but others remain. In most recent cases where the Brussels Regulation has featured, the company proposing the scheme has been able to provide expert evidence that the scheme would be recognised in the relevant EU jurisdiction(s), whether the Brussels Regulation applies or not. Therefore it seems unlikely that a Brexit would have a significant effect on the popularity of schemes.

In any event, change is coming…

While the consequences of Brexit should not be catastrophic for the flourishing UK R&I industry, this is not a time for complacency. There is a global drive to improve the effectiveness of existing national regimes and international frameworks. Numerous EU states have already introduced reforms to provide for more flexible restructuring procedures (some modelled on the UK scheme) and the EU Commission is expected to publish a minimum standards directive by the end of 2016, which could be a significant step towards harmonisation of restructuring and insolvency laws in Europe. Harmonisation is certainly not a foregone conclusion: it raises many complex issues. What is clear is that the market is becoming more competitive and, Brexit or not, more change is coming.

14. Data protection

For the foreseeable future, the UK seems likely to stick with a regime requiring standards of protection for personal data that are materially the same as those under the EU regime

Although there remains significant uncertainty around the effects of Brexit, it is likely that whatever the outcome of the referendum the UK will maintain a data protection regime materially compliant or consistent with EU regulation. As a result, UK businesses should plan to continue to comply with the EU regime, including the forthcoming changes to that regime through the new EU General Data Protection Regulation ("GDPR").

Data protection in the UK

The key pieces of legislation that form the current data protection regime in the UK derive principally from the EU data protection rules:

i. the Data Protection Act 1998 ("DPA") governs the collection and use of personal data and implements the Data Protection Directive[33];

ii. the Privacy and Electronic Communications Regulations 2003 (as amended) ("PECR") provide specific privacy rights in relation to electronic communications and implements the e-Privacy Directive[34]; and

iii. the Regulation of Investigatory Powers Act 2000 ("RIPA") consolidates and updates a range of law enforcement investigative powers and ensures compliance with the UK's obligations under the European Convention on Human Rights ("ECHR").

The current European data protection regime will most likely be replaced by GDPR which would apply directly to all EU Member States in early-mid 2018 (discussed further below).

General Data Protection Regulation

On 15 December 2015, the EU Parliament and Council of the EU reached provisional agreement on the GDPR. Once formally adopted, which is expected to be early to mid-2016, the GDPR will come into effect two years thereafter, likely to be early to mid-2018.

The GDPR will replace the Data Protection Directive and the national data protection laws of the Member States will become obsolete. The GDPR will retain the core principles of the current regime but is intended to introduce a harmonised regime across the EU. It will introduce new obligations and higher sanctions, and for many organisations will require a significant shift in their approach to handling and using personal data. The GDPR has a wide extra-territorial application. As a result, the EU data protection regime will be relevant to a larger number of businesses than at present.

[33] EU Directive 95/46/EEC on the protection of individuals with regard to the processing of personal data (the "Data Protection Directive").
[34] Directive 2002/58/EC of 12 July 2002 concerning the processing of personal data and the protection of privacy in the electronic communications sector (the "e-Privacy Directive").

When the GDPR becomes law, it will apply to all organisations established in the EU that process personal data and to organisations established outside the EU, if they process personal data relating to the offering of goods or services to individuals in the EU or if they monitor the behaviour of individuals in the EU, for example, through the use of cookies. Non-EU based organisations who process personal data in this manner will be covered by the GDPR and will need to review and adapt their data protection practices and procedures to ensure compliance with the GDPR. In addition, the GDPR would also apply in the EEA countries when it is incorporated into the EEA Agreement.

Effect of the different exit models

As for other areas of law, the effect of Brexit on the data protection regime would vary depending on the model for exit that is adopted:

i. If the UK exits the EU but remains a member of the EEA and EFTA, the GDPR would apply once it is incorporated into the EEA Agreement. Thus, UK-based companies processing personal information would still have to comply with the EU data protection regime, most likely the GDPR. Further, there would likely be a continuing requirement for the UK to implement the e-Privacy Directive in UK law.

ii. If the UK exits the EU and joins the EFTA but not the EEA, or if it does not join EFTA, the GDPR will only apply to UK-based businesses that process personal information relating to the sale of goods and services to individuals in the EU or the monitoring of individuals' behaviour in the EU. The e-Privacy Directive would no longer have to be implemented in UK law. The UK courts would also no longer be required to follow the jurisprudence of the EU courts.

Would the UK legislate away from the European Data Protection Regime?

If the UK left the EU and did not join the EEA, there is a question of what the UK would do to its data protection regime. It is likely that the UK will, for the foreseeable future, stick with a regime requiring standards of protection for personal data (and imposing consequential restrictions and obligations on data controllers) that are the same as or materially similar to those imposed by the EU regime. This briefing suggests four reasons why this will be the case.

Multinational companies seek to implement global compliance standards

Multinational companies generally seek to implement a single global set of compliance standards across their various businesses to ensure that the organisation complies with the highest standard required globally. By having one set of compliance standards, organisations eliminate the need to implement different policies to satisfy different compliance requirements across different jurisdictions.

As the EU imposes one of the strictest data protection regimes in the world, many multinational businesses seek to comply with the EU data protection regime to ensure global data protection compliance. Thus Brexit is unlikely to alter multinational companies' approach to data protection compliance, as they will continue to comply with the EU regime in any event, regardless of what the UK legislates for its domestic businesses. Further, if the UK's multinationals comply with an EU-led set of standards, they are likely to place pressure on the UK Government to maintain those standards as the basis for the UK's own data protection laws.

UK businesses will need continued access to EU data

Under the EU data protection regime, personal data may only be transferred outside the EEA to countries thst ensure an “adequate level of protection” for the data. The European Commission can designate a country as having an adequate level of protection.

If the UK leaves the EU and does not join the EEA, it is likely that it would apply to the European Commission to be designated as an “adequate” country (to achieve this, it would need to maintain the same or materially similar laws to the EU’s Global Prohibition Regime (“GPR”) regime). If the UK does not do so, or if it chooses to deviate from the EU data protection regime, data transfers to the UK would only be compliant if model clauses or binding corporate rules were used[35]. In those circumstances, UK organisations would need to re-think their data protection compliance strategy and documentation for data transfer.

The UK has an established culture of data protection

The UK data protection regime is well established and accepted in the UK. The UK has had data protection provisions in place for over thirty years and, in a sense, the current regime is viewed by data subjects in the UK as being a UK, rather than EU, regime. Any amendment to the regime that would result in a reduction in the level of protection afforded to individuals’ personal data would likely be opposed by the general public. It would be a fairly bold (and potentially unpopular) move for a UK government to reduce the standards of data protection and to deviate from the European harmonised approach.

There is general UK support for the new GDPR

The UK has been generally supportive of the GDPR and there have been no major indications that the UK disagrees with the EU approach to data protection or that it wishes to reform the regime.

The Information Commissioner’s Office (“ICO”) (being the UK statutory regulator of the data protection regime) published commentary on the European Council’s June 2015 draft of the GDPR, highlighting elements of the GDPR that it felt required improvement during the negotiations process[36]. The final draft of the GDPR addressed most of the ICO’s concerns. The ICO’s ultimate aim was to ensure that the GDPR is clear, simple and easy to understand. The ICO’s commentary does not suggest that it would seek a major change to the UK’s own data protection regime, in the event that Brexit freed the UK from the underlying EU legislation.

The UK has historically adopted a slightly more lenient approach to the interpretation and enforcement of the EU data protection regime than some other Member States, which have taken a more prescriptive approach. If the UK left the EU and did not join the EEA, it could adopt a more flexible approach to the interpretation of the data protection rules, as the UK courts would no longer be obliged to follow EU jurisprudence and we may over time see a divergent approach in practice between the UK and the EU. However, the ICO has not indicated that it would prefer to adopt a more lenient data protection regime, and it is certainly too early at this stage to predict that a wholesale retrenchment away from the EU model and standards of data protection would flow from Brexit.

[35] For the effect of the *Schrems* decision (Case C-362/14 *Maximillian Schrems v Data Protection Commissioner*) on these alternative mechanics of transfer, please see our publications: ‘The Harbour is no longer safe…’; ‘EU regulations weigh in’; and ‘EU-US Privacy Shield to replace US Safe Harbour’.

[36] Available at https://ico.org.uk/media/1432420/ico-analysis-of-the-council-of-the-european-union-text.pdf.

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