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BREXIT: PREPARING FOR A NO DEAL SCENARIO

Once considered the "cliff edge", the possibility of the UK exiting from the EU without agreeing a trade deal has moved from the unthinkable to increasingly likely. Both sides are ramping up preparations for a 'no deal' scenario, which would have significant implications for businesses in all sectors. We have identified the key challenges that you should be considering as part of your Brexit strategy:

CUSTOMS

1.1 Under a 'no deal' scenario trade in goods between the UK and the EU will operate under WTO rules. As a result there will be no preferential treatment for goods moving from the UK into the EU (and vice versa) and individual tariffs on goods would apply (ranging from 0% to approximately 30%), along with import VAT. Customs declarations, which are not currently required, will have to be submitted on movements between the UK and EU-27 which will lead to additional administrative burdens on companies and might lead to imports/exports being slowed down.

1.2 The impact that these changes will have on businesses will be significant. A report produced by Baker McKenzie on the 'Realities of Trade after Brexit', found that a 'no deal' scenario could cost the UK's Automotive, Technology, Healthcare and Consumer Goods sectors a total of almost £17 billion per year in lost EU export revenues[1].

1.3 Finally, the UK will lose the benefit of the Free Trade Agreements (FTAs) that the EU has concluded with third countries which give EU goods preferential access to these markets. This will mean that exports from the UK to these countries and imports from these countries into the UK will face additional duties unless the UK manages to enter into similar, or possibly interim, agreements with these countries to allow preferences to continue.

PRODUCT REGULATION

2.1 Under a 'no deal' scenario, we expect that the UK Government will maintain its plan to incorporate the current body of EU product regulation into UK law by way of the Great Repeal Act. This means that the UK would stay aligned to EU product-related laws for the immediate period after Brexit.

2.2 There are significant questions, however, about how this plan will operate. Presumably, for products coming into the UK, the UK Government will act unilaterally to recognise products conformed under EU procedures as being compliant for the UK market, such that a CE-marked product, for example, does not need to undergo any different assessment or marking for the UK. This would be the least burdensome option for both international and UK manufacturers and distributors who supply to both EU and UK markets.

2.3 For products already placed on the EU market at the date of withdrawal but not yet sold through to end-users, we expect these will be permitted to continue to be made available in both markets. In fact, the EU Commission has already recommended that any product lawfully placed on the EU market before the UK's withdrawal should, after the withdrawal date, be permitted to continue to be made available on the market of the UK or the remaining EU-27. The UK Government echoed this in its position paper, published in August 2017 on "Continuity in the Availability of Goods for the EU and the UK".

2.4 Beyond these general points, in the absence of any agreement to the contrary UK entities would no longer qualify as EU-based "manufacturers", "importers", "authorised representatives" or "responsible persons" for the purpose of product-related laws. UK Notified Bodies would lose their status as EU Notified Bodies and be unable to perform conformity assessment tasks. Similar issues arise in more highly regulated product sectors, such as food, cosmetics and medical devices/pharmaceuticals. Businesses that have a UK-based company or UK individual designated as the required responsible entity for the EU, such as the Food Business Operator in the food industry or the Responsible Person for cosmetics, will have to be move that function to the EU-27, unless dealt with otherwise in a separation agreement.

2.5 The EU REACH chemicals regime is potentially one of the more problematic areas in a 'no-deal scenario' because of the crucial role of the European Chemicals Agency (ECHA) in registering chemical substances. The UK cannot unilaterally decide to remain part of REACH and would need an agreement with the EU to allow it to continue to participate. The Government has a plan to introduce a UK equivalent of REACH and build a domestic capability to enable registration of chemicals in the UK following withdrawal. Exactly how the UK regime will work, and how it will interrelate with the EU REACH regime, is unclear. Similar points can be made in respect of various other EU chemical regimes which involve EU-wide procedures (e.g. the Biocidal Products Regulation, the Cosmetic Products Regulation).

2.6 Another question is the UK's continued participation in the RAPEX system under the General Product Safety Directive (or its intended successor under the EU's Consumer Product Safety and Market Surveillance package). The

[1] *See here https://www.bakermckenzie.com/-/media/files/insight/publications/brexit_tradeflows.pdf?la=en.*

RAPEX system facilitates speedy exchange of information between jurisdictions about unsafe products. With no agreement with the rest of the EU-27, the UK would be unable to participate in RAPEX post-Brexit, disconnecting UK product safety authorities from the rapid information exchange that occurs between EU countries when dangerous products are found on the market. This could compromise UK consumer safety unless an effective solution is found.

2.7 Looking longer term, there is a major practical concern about UK product-related laws drifting out of alignment with the EU, given the regularity with which EU product laws are amended and updated. The UK would be free to decide to what extent it wants this to happen. In fact, it could relax regulatory requirements in some areas, or recognise other countries' systems (e.g. US product standards), alongside EU product laws.

SERVICES

3.1 Under a 'no deal' scenario the UK will be trading services with the EU on the basis of WTO rules which would provide less favourable trading conditions than membership of the Single Market or a FTA. The aim of the WTO rules as set out in the WTO's General Agreement on Trade in Services (GATS) is to remove any restrictions and internal governmental regulations in the area of services delivery that are considered 'barriers to trade'.

3.2 In practice, this means that in certain sectors there will be additional regulatory requirements and standards for trading in services which will increase compliance costs and may even prohibit the provision of certain services between the EU and the UK. However, in other sectors, even under a 'no deal' scenario, there should be limited to no restrictions on the provision of services from the UK to EU-27 (and vice versa). The exact impact for your business will therefore depend on the specific sector in which you operate.

3.3 Additionally some of the FTAs that the EU has concluded with third countries give EU services preferential access to these markets (for example the EU-Canada FTA). Upon leaving the EU, UK service providers will lose such preferential access, unless the UK manages to enter into similar agreements with these countries.

3.4 The impact on financial services businesses of a no-deal will depend on their nature. The EU retail financial services market shows relatively little cross-border activity and this reflects cultural, national preferences and consumer choice. As such these firms are less reliant on passporting their services so the impact is likely to be less than compared with wholesale markets which are more integrated across Europe. In respect of the latter, the impact on firms doing cross border business (into the EU-27 or the UK) should not be underestimated.

3.5 Subject to what "access" may be negotiated, departure from the Single Market will therefore mean the loss of passporting rights for UK based firms and loss of status as EU "credit institutions", "investment firms" and "insurance undertakings". UK firms will become third country firms, that is firms with their head or registered office in a jurisdiction outside the EEA. The UK may potentially be in no better position to access the EEA market than say, a US or Australian firm. The precise impact will depend on the nature of the business concerned. For example, domestic retail financial services may be least affected, while in contrast, funds, such as UCITS, being the most. Some business may be able to put in place "workarounds", such as booking business to certain jurisdictions and using back-to-back transactions. In some sectors it may be possible to continue to access the Single Market on the basis of equivalence of the rules (e.g., under MiFID II, MiFIR and EMIR) – although this would require EU recognition and would not be automatic.

3.6 Firms will require new authorisations and face closer regulatory scrutiny in respect of their cross border business. Lead times for creating new subsidiaries and seeking regulatory approval can, at a minimum, extend from 6 to 12 months. What is true for UK firms accessing EU-27 markets will apply equally to EU-27 firms and their access to the UK market.

3.7 There may also arise issues over contract continuity. On withdrawal, UK-based firms will no longer be able to service existing cross-border financial contracts in the EEA. Similarly, for EEA providers which have existing financial contracts with UK-based parties. Many sectors will potentially be impacted including insurance, pension schemes, medium and long-dated derivatives contracts, revolving credit facilities, and possibly customer terms of business, prime brokerage and custody arrangements. The UK authorities have committed to put in place a temporary permissions regime and measures in respect of contract continuity in the event of a no-deal. However, to date there has been no reciprocal commitment by the EU-27.

PEOPLE

4.1 EU/EEA citizens are currently living /working in the UK under the EEA Freedom of Movement Regulations so as these would come to an end on 31 March 2019, a no deal Brexit means that EU/EEA citizens could find themselves without immigration status in the UK. Since the Home Office has already invested significant resources in the new system for the transitional period under the Withdrawal Agreement it is likely (although not confirmed) that the new system would still be implemented to avoid the chaos of allowing EU/EEA citizens to default into the existing UK immigration system.

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