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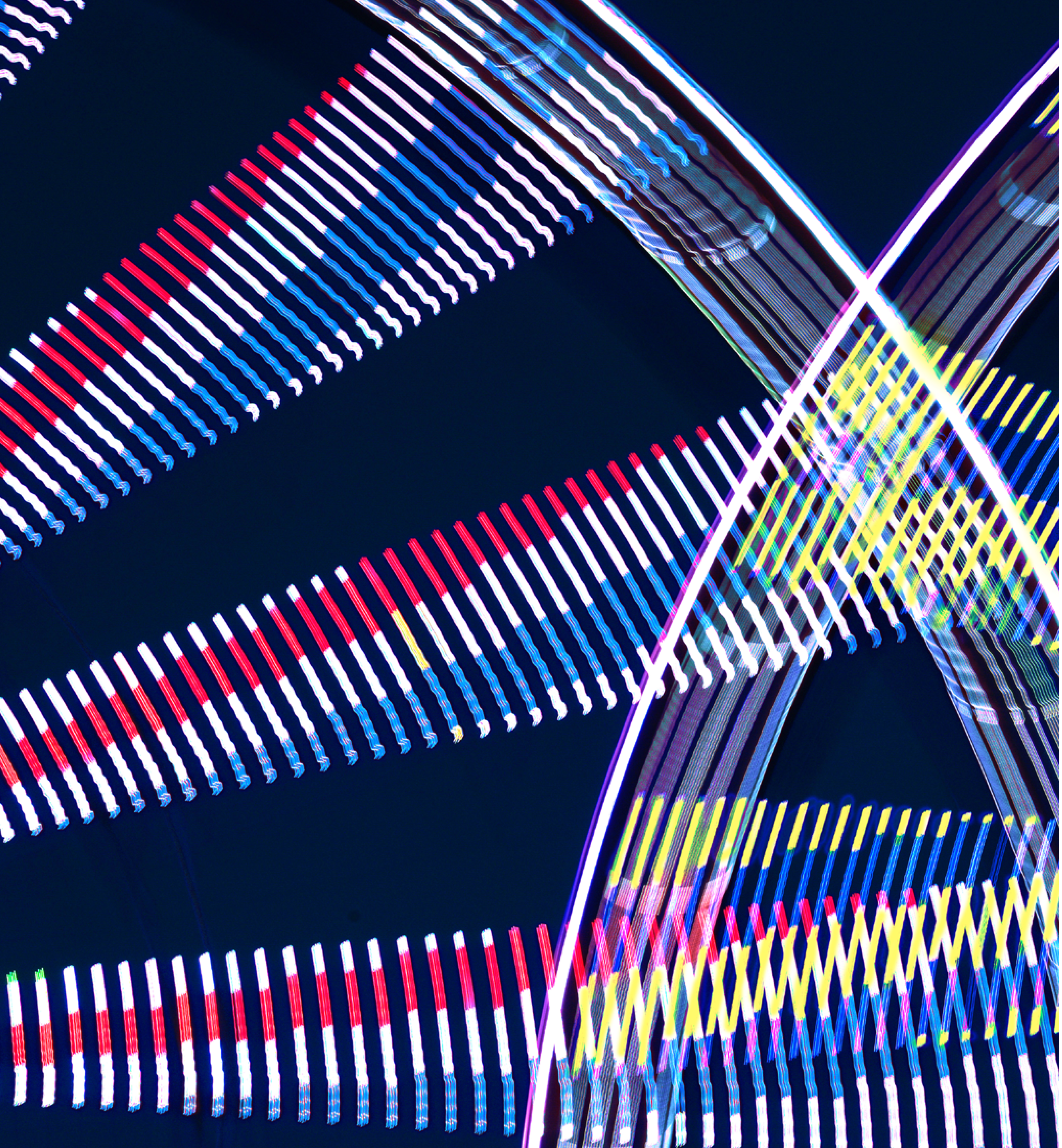
Brexit: Key Implications for the Industrials, Manufacturing and Transportation Sector



Key Implications for Business

The new EU-UK Trade and Cooperation Agreement (TCA) created a new relationship between the EU and UK from 1 January 2021. Now that we know the terms of this deal, Industrials, Manufacturing and Transportation (IMT) businesses need to review their Brexit planning as they continue to prepare for the key challenges ahead.

What should IMT businesses think about to prepare for the post-transition period? To help you get started, we have identified a number of key areas that have changed as of 1 January 2021, and some practical considerations so that you can address specific impacts on your business.

The global nature of our Firm and the clients we represent means that we have a number of experts who can provide advice that is tailored to your organisation and the challenges that you face. If you would like help navigating the complicated, evolving landscape, please contact a member of our dedicated team of specialists (contact details below) or your usual Baker McKenzie contact. Additionally, for further analysis of more general key legal and regulatory issues resulting from Brexit that will likely apply to all IMT businesses, please see our **Brexit Deal Checklist: Key Implications for Business**.

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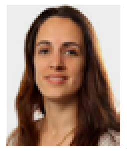

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Supply Chains

Key issues

- Companies in the IMT sector have some of the most complex supply chains of any sector and, thus, they are particularly susceptible to the impact of the new TCA on supply networks and the movement of raw materials, parts and finished goods.
- Although the TCA removes customs tariffs on imports of "originating" goods (i.e. goods that wholly originate in or are substantially worked or processed in the UK or EU), it also introduces new customs formalities for all goods that cross the EU/UK border. These formalities include new customs controls, including rules of origin and the payment of import VAT. The risk of delays in clearing customs could disrupt manufacturing operations and delivery to customers, affecting sales and revenue. As a result, IMT companies will experience costs and financial and administrative burdens related to the movement of goods between the UK and the EU.
- The movement of controlled goods between the EU and the UK, and from the UK to non-EU countries, will also be subject to new export licensing requirements.
- Companies responding to supply chain challenges by changing manufacturing locations or suppliers may be able to alleviate the risk of delays but it may also increase other compliance, quality assurance and commercial risks as a result of new supplier relationships.

Recommendations

- Conduct a full supply chain assessment including where manufacturing takes place and where parts and finished products are moved from and to (including third countries, the UK and the EU).
- Develop contingency plans for mitigating against delays and supply chain bottlenecks, such as stockpiling and identifying additional suppliers for critical locations or components.
- Expand supply chain and customs expertise and resources, with consideration of both personnel and technology needs, such as digitalisation, blockchain and other tools for managing customs administration and supply networks.
- Calculate additional duties and corresponding financial and revenue implications based on the specific rules of origin applicable to your products, and consider mitigation strategies.
- Determine whether importer entities or representatives need to be established in the UK and/or the EU and whether other organisational changes are required to adapt to new export licensing requirements.

Automotive Subsector

Key issues

- The automotive industry is illustrative of many challenges that all IMT subsectors now face, with implications for both the UK and the EU automotive industries. The impacts will extend to vehicle manufacturers, suppliers of systems and components and, ultimately, consumers. Approximately 85% of passenger vehicles imported into the UK come from the EU, representing about one-third of the EU's exports. While only 20% of the EU's auto imports are from the UK, this represents approximately half of the UK's auto exports.
- Fortunately, with regard to the new rules of origin in the TCA, there are certain transitional product-specific rules for hybrid and electric vehicles that allow a greater proportion of non-originating material to be included in products exported under preference. The transitional measures are in effect until 31 December 2026 and allow businesses time to assess the materials used when manufacturing vehicles.
- Under the EU's single market, the automotive industry employed complex just-in-time supply chains, and vehicles and parts moved freely. The industry is concerned that the significant effort required for companies to navigate the new EU-UK relationship will divert resources away from investments in technology and other strategic initiatives to advance the automotive industry.
- The sector will now have the added administrative burden of customs declarations. Duties and tariffs will be imposed on vehicles and parts, and the sector will have the added administrative burden of customs declarations. These changes will affect costs and increase the risk of delays in production and the delivery of parts and vehicles. Many automotive companies have responded by stockpiling parts and adjusting supply chains to domestic sources.
- EU rules for the automotive industry only apply in the UK to the extent they are "retained EU law" and implemented into UK law. The TCA provides for regulatory convergence and agrees that the World Forum for Harmonisation of Vehicle Regulations within the framework of the United Nations Economic Commission for Europe is the relevant international standardising body. This means that both parties must accept products covered by valid UN type-approval certificates, without further testing or marking requirements to verify compliance, thereby providing some relief from the existence of two regulatory schemes.

Recommendations

- Carefully evaluate supply chains for automotive components and systems, including the movement of goods and the location of manufacturing to identify potential risks of bottlenecks, delays and shortages.
- Analyse existing commercial agreements with automotive parts suppliers and other third parties and consider the feasibility of addressing Brexit implications in contractual relationships.
- Determine the financial impact of duties and tariffs, as well as additional costs of changes in suppliers and administrative burdens of customs procedures, and consider possible cost mitigation measures.
- Evaluate the need to appoint a representative to conduct actions in the EU and seek the transfer or re-registration of approvals and certificates needed to place vehicles on the market in the EU.

Chemicals Regulation

Key issues

- As a result of Brexit, chemicals are subject to duplicate regulatory schemes as of 1 January 2021, with impacts on the chemicals subsector, as well as "downstream" subsectors that use regulated chemicals (including many IMT subsectors such as automotive, aviation, plastics, industrials and agribusiness).
- Prior to Brexit, chemicals were regulated under the EU Registration, Evaluation, Authorisation and Restriction of Chemicals (REACH) legislation, which required the registration of chemicals before they are placed on the market. As of 1 January 2021, UK companies no longer hold valid registrations under the EU REACH and companies that manufacture, import, sell or distribute chemicals in the UK and the EU now need to comply with both UK REACH and EU REACH rules.
- The UK REACH regime is effectively the same as the EU REACH regime, and UK regulations provide for the automatic transfer of existing EU REACH registrations held by UK entities into the UK REACH system. However, because the UK will not be able to access EU registration data, this information will need to be resubmitted in the UK. Further, UK companies exporting to the EU will not be able to rely on UK REACH registrations and will need to transfer their EU REACH Registrations to EU entities or appoint an EU "Only Representative". British companies importing chemicals from the EU will face new registration requirements under UK REACH.
- The TCA commits the EU and UK to implement the United Nations Globally Harmonized System of Classification of Labelling of Chemicals, which they (and many other countries) do already, and provides for related cooperation and information exchange.
- IMT companies should expect similar issues related to other EU chemicals legislation, such as the Biocidal Products Regulation and Prior Informed Consent Regulation, which will no longer apply to UK companies.

Recommendations

- Take actions to transfer chemical registrations from the UK to the EU and establish representatives or business entities as needed in the EU.
- Evaluate supply chains across EU and UK operations and compare against REACH registrations to determine where action is needed to comply with applicable chemical regulatory schemes in all jurisdictions.
- Address risks inherent in complying with duplicative chemical regulatory schemes, including establishing processes to ensure consistency in data and information gathering and submittals.
- Consider options for alleviating impacts to supply, such as building a reserve of raw materials to minimise disruptions in production.

Aviation Subsector

Key issues

- Given the nature of air travel and the international agreements and regulatory schemes specific to aviation, the sector faces significant change under the new EU-UK relationship. From 1 January 2021, EU and UK airline operators are third country operators in the respective airspaces.
- Before Brexit, EU and UK carriers benefited from the single EU airspace. Under the TCA, EU and UK operators will have less generous operating rights; for example, UK operators with a UK licence will not be able to operate intra-EU flights and vice versa.
- The US and the UK have struck an open skies agreement that applies from 1 January 2021, replacing the EU- US agreement that previously covered the UK.
- EU aviation security rules no longer apply in the UK, including rules related to aircraft, passengers, baggage, and cargo security and screening. UK passengers must go through passport control when flying into the EU, as must EU passengers flying into the UK. The UK also no longer participates in or influences the standards made by the EU Aviation Safety Agency.
- UK air carrier operating licences are no longer valid in the EU and carriers must separately ensure compliance with both EU and UK rules for air carriers. Airlines must be majority EU-owned in order to hold an operating licence from a licensing authority of an EU member state and to be able to fly between EU countries. Further, certificates of airworthiness, pilot licences and numerous other certificates for aircraft and aviation personnel authorisations held in the UK no longer apply in the EU unless transferred or separately obtained.
- The US still recognises the validity of previously certificated UK carriers operating to and from the US and it intends to reissue certificates to those UK carriers. This allows existing UK carriers to continue to fly to the US, even if they are owned and substantially controlled by EU interests. New applicants are required to be owned and substantially controlled by UK interests.

Recommendations

- Take steps to ensure aircraft and aviation personnel comply with EU requirements and certificates, including transferring UK certificates to the EU and establishing EU ownership.
- Businesses and individuals not in the aviation industry may also be impacted and they should prepare contingencies for possible travel disruption, including the movement of both passengers and cargo. Airlines have expressed their commitment to ensuring that air travel runs smoothly, but they are also in the midst of addressing disruption and reduced demand due to the continuing COVID-19 pandemic.

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