WILLIAM FRY

BREXIT BUSINESS BRIEFING

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In this edition of the William Fry Brexit Business Briefing, our Brexit Group analyses the key issues for business arising from Theresa May's announcement of key elements of the UK's negotiating position.

BEYOND "BREXIT MEANS BREXIT"?

After months of uncertainty about what the UK will seek in negotiations on its departure from the EU, on **17 January 2017**, the **UK Prime Minister, Theresa May**, announced the UK's twelve main negotiation objectives namely:

1	Provide maximum certainty throughout the exit process.
2	Regain control over laws and withdraw from the jurisdiction of the European Court of Justice ('ECJ').
3	Strengthen the Union between the different components of the UK.
4	Preserve the Common Travel Area with Ireland.
5	Control the number of EU migrants.
6	Agree an early guarantee of the rights of EU citizens in Britain and British citizens in the EU.
7	Protect and build on existing workers' rights.
8	Conclude a comprehensive UK/EU free trade agreement – with the UK outside the Single Market but with a UK/EU customs arrangement.
9	Pursue new UK free trade relationships across the globe.
10	Cooperate with the EU on science, research and technology.
11	Cooperate with the EU in foreign affairs, defence and combatting terrorism and crime.
12	Agree appropriate transitional exit arrangements.

These twelve objectives represent the UK's opening negotiation position, but it is unlikely that all of these objectives will be achieved. Unfortunately there will continue to be much uncertainty surrounding the UK's relationship post-Brexit, not just with the EU, but with other major trading blocs also. However it does seem increasingly likely that the UK is heading for a so called hard Brexit.

WILLIAM FRY'S ANALYSIS OF KEY ISSUES FOR BUSINESS

What is the UK's position and what is the EU's anticipated response?

Theresa May confirmed on 17 January 2017 that the UK plans to leave the Single Market.

This position is based on a pragmatic acknowledgement by the UK that the EU will not alter its fundamental position that membership of the Single Market is conditional upon accepting free movement of goods, services, capital and people and the jurisdiction of the ECJ. Neither free movement of people nor the jurisdiction of the ECJ is currently acceptable to the UK.

How will this affect business?

The answer to this question will depend on the sector in which the business operates. However, the sector most immediately affected is expected to be financial services.

When the UK leaves the Single Market, many UK regulated financial services firms will no longer be able to passport their services into the EU (and vice versa) and they risk losing access to EU markets and clients.

Many UK regulated financial services firms are now expected to activate their Brexit contingency plans in Q1 and Q2 2017 by establishing an alternative EU base in another EU Member State (such as Ireland) and obtaining regulatory authorisation there. This will enable them to guarantee continuity of access to EU markets and clients after the UK leaves the Single Market.

CUSTOMS UNION

What is the UK's position and what is the EU's anticipated response?

Theresa May confirmed in her speech that the UK does not want to be a full member of the Customs Union. This is grounded on the fact that full membership of the Customs Union would preclude the UK from negotiating its own trade agreements with countries outside the EU. However, Mrs May also confirmed that the UK will seek a customs arrangement with the EU involving reciprocal tariff-free trade.

It is challenging to see how the EU will agree to the type of customs arrangement that the UK is seeking - one that allows the UK to enter into its own arrangements with countries outside the EU on core issues such as the level of external tariffs and quotas while retaining internal tariff-free trade within the EU.

How will this affect business?

If the UK leaves the Customs Union and it fails to reach agreement with the EU on a customs arrangement involving reciprocal tariff-free trade, this would mean that trade between the EU and the UK would be subject to greater restrictions and tariffs when the UK leaves the EU.

Such an outcome would be likely to:

- Have a disproportionately adverse effect on sectors where there is particularly heavy trade in goods between the UK and EU Member States, including the automobile, energy, agriculture and food/drink sectors. The Irish Department of Finance has estimated that the UK leaving the Customs Union could lead to a 30% decline in Irish exports to the UK; and
- Complicate achievement of the UK's separate objective of preserving the Common Travel Area between the UK and Ireland – at a minimum necessitating a soft border for the purpose of customs controls (e.g. "frictionless" electronic customs controls).

TRANSITIONAL EXIT ARRANGEMENT

What is the UK's position and what is the EU's anticipated response?

Theresa May confirmed on 17 January 2017 that the UK will seek some form of transitional arrangement (or "implementation phase") that would avoid a sudden "cliff edge" Brexit that would be disruptive for business.

However, challenges facing the UK in achieving this objective include that:

- The EU is expected to insist that the UK would remain subject to the jurisdiction of the ECJ during any transitional phase and it is unclear whether the UK would accept this;
- The possible lack of incentives for the EU to agree to a transitional arrangement without the UK continuing to contribute substantial sums to the EU budget - which in turn may be unpalatable to the UK; and
- Possible delay in reaching agreement on transitional arrangements which may limit the benefit of such arrangements to UK-based firms.

How will this affect business?

If early agreement is reached on a transitional arrangement for the UK's departure from the EU, this would:

- Soften the impact of Brexit for business; and
- Encourage some UK regulated financial services firms to postpone implementing their contingency plans to establish an alternative EU base in another EU Member State.

However, while many businesses may welcome some form of transitional arrangement, the longer it takes to agree transitional arrangements, the more likely it is that UK regulated financial services firms will be left with no option but to activate their plans to establish an alternative EU base in another EU Member State (such as Ireland) given the imperative of safeguarding access to EU markets and clients.

EU/UK TRADE DEAL

What is the UK's position and what is the EU's anticipated response?

One of the UK's twelve negotiating objectives is to conclude a comprehensive UK/EU free trade agreement. However, Theresa May concluded her speech of 17 January 2017 by making clear that the UK considers:

- That no deal is better than a bad deal for the UK;
- That if a satisfactory deal is not reached the UK reserves the option of changing its tax rates and its business model - a clear challenge to the EU; and
- That the UK believes the risks of no deal being reached are greater for the EU than for the UK.

Again the UK faces several challenges in achieving its stated objective in this area, including:

- That Michel Barnier - chief negotiator for the EU in the negotiations on the UK's exit from the EU - responded to Theresa May's speech by repeating the mantra "divorce first, trade talks after"; and
- Many experienced diplomatic and trade experts have warned that reaching a relatively complex trade deal, such as one between the UK and the EU, could take up to ten years and even then there is no guarantee that it would be ratified by all EU Member States.

How will this affect business?

If an EU/UK trade agreement is not reached:

- Trade between the EU and the UK would be subject to greater restrictions and tariffs when the UK leaves the EU - there is a risk of reversion to WTO rules and common tariff schedules for EU/UK trade when the UK leaves the EU; and
- Again, this would have a disproportionately adverse effect on sectors where there is particularly heavy trade in goods between the UK and EU Member States, including the automobile, energy, agriculture and food/drink sectors. If the UK leaves the Customs Union and WTO rules are applied exports of meat from Ireland to the UK will be subjected to a 50% tariff and dairy to a 25% tariff.

WHY ARE UK FIRMS CHOOSING IRELAND AS AN ALTERNATIVE POST-BREXIT BASE?

Ireland has strong advantages over other EU Member States, and offers the least disruptive option for UK firms seeking to establish an alternative post-Brexit EU base. These are some of the reasons to choose Ireland:

- Attractive corporation tax rate (12.5%)
- Only English speaking country in the EU after Brexit
- Fastest growing economy in the EU
- Pro-business environment
- Strong commitment to EU membership
- Similar employment laws to the UK
- Common law jurisdiction with similar legal system to the UK
- Highly skilled and educated workforce
- R&D incentives
- Guaranteed passporting rights to EU markets
- Comprehensive tax treaty network
- Low start up regulations and ease of establishing a business
- Geographic position close to the UK and same time zone as the UK
- Stable labour costs