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Brexit: Issues and Q&A for Businesses

On Thursday 23 June 2016, the UK electorate voted to leave the European Union. While this vote was advisory in nature, we expect that the UK Government and Parliament will respect the outcome and serve notice to terminate the UK's membership of the EU. This will start a negotiation of the terms of both the UK's withdrawal from the EU and the framework for its new relationship with the EU and its other trading partners. This memorandum focuses on some of the main legal and commercial impacts of the UK's proposed exit across a broad range of commercial and industrial areas where UK business may be impacted or English law is used.

We start with a brief look at the UK legal basis for incorporation of EU law and constitutional issues, and then analyse the impacts of Brexit in the context of specific commercial issues: M&A, capital markets, finance, derivatives, funds, tax and privacy. This is aimed to be relevant for businesses in finance, manufacturing, export, retail, defence, energy and other industries. Our separate note published on 24 June addressed certain key financial regulatory issues, and a note dated 21 March discusses the various options for a post-Brexit UK-EU relationship. This note also considers the withdrawal process under Article 50 of the Treaty on European Union (the Lisbon Treaty) and the possible ramifications for Scotland and other parts of the UK.

European Law in the UK: How It Works Now and What Will Change

How Is European Law Currently Given Effect in the UK?

The UK comprises three separate legal jurisdictions which participate in the European Union: England & Wales, Scotland, and Northern Ireland. Where we refer here to "UK laws" (a misnomer), we refer to all of them. Gibraltar, an overseas territory of the United Kingdom, is also subject to some aspects of European Union law and will also be affected by Brexit.

European law is given effect in the UK under the European Communities Act 1972 ("ECA"). This:

- Gives legal force to the Treaty on the Functioning of the European Union;
- Gives appellate powers to the European Court of Justice ("ECJ");
- Makes EU Regulations directly applicable;
- Allows EU Directives to be implemented by secondary legislation; and
- As was later held by the English Courts, has the result of disapplying English and other UK laws to the extent that they conflict with EU laws.

How Can the Current Legislation Be Amended?

The ECA contains no provision allowing for fundamental amendments by way of secondary legislation. Material amendments have in the past only been made by Act of Parliament. For example, the European Union (Amendment) Act 2008 was introduced to give effect to the Lisbon Treaty. This legislation will need to be explicitly amended or repealed as part of any Brexit. To do so will need a new Act of Parliament. Given that most MPs and members of the House of Lords support "Remain," this may present practical difficulties. However, we would expect most of the major parties to respect the referendum outcome unless it is superseded by other events, such as EU reform, a general election and/or a new referendum.

What Are the Options for Amendment?

There are various options as to what to do with the ECA. The way in which it is done will have different ramifications for all those subject to European laws and living or operating in the UK. The following options assume the scenario of a full exit (e.g. with no new arrangement dealing with the continued applicability of EU law being established):

- **Option 1: EU Exit and Complete Repeal and New Legislative Programme**. This would result in all European laws, including those made prior to the date of exit ("E-Day," which is expected to be September 2018 at the earliest) being invalid and of no further effect. Legislators could even go further and provide that previous decisions of the European court be disregarded so that they have no binding effect under UK laws. In areas where the UK wishes to fill the legislative void, new UK legislation would be required. Some such new legislation would fall under the competence of the Scottish and Gibraltar Parliaments or the Welsh and Northern Irish Assemblies. This option is likely to involve a lot of legal work and considerable parliamentary time, so is probably not immediately practicable.
- **Option 2: EU Exit with Grandfathering of Existing Rights**. The ECA 1972 would remain effective for the period prior to E-Day, but cease to have effect thereafter. European laws made prior to this date would continue in effect. This approach will be simpler and will likely lead to less uncertainty. It is how we would see any Brexit involving leaving the single market likely being managed. There would be an interesting question as to whether ECJ decisions relating to grandfathered legislation, particularly decisions taken after 2018, should have effect, whether the entire EU jurisprudence would be abandoned or whether it would have some status as a point of reference. Similarly, the status of EU laws which were made prior to the date of exit but which, on their own terms, must be implemented by Member States after 2018 will need to be clarified. A process of "take and tailor" could then apply to new EU laws going forwards and existing EU laws could be tweaked as desired. A similar process has taken place, at various times, in Hong Kong, Singapore, and most recently in the Abu Dhabi Global Market (which continues to apply the English common law as it develops, rather than only on a snapshot basis—you might like to view our client note which is available here). This option could involve different approaches to different types of legislation, with some areas kept largely the same, whilst others are promptly amended. The Financial Conduct Authority ("FCA") has already indicated its preference for this kind of grandfathering approach as regards its rulebook.
- **Option 3: UK Remains in the Single Market**. If the UK opts to remain in the single market, for example by joining the European Economic Area ("EEA"), the ECA 1972 will need amendment (for example, as regards the extent of the supremacy of the ECJ) but otherwise the legislative arrangements will remain undisturbed.

Withdrawal and Framework for Future Cooperation

What Is the Process for the UK Withdrawing from the EU?

On 23 June 2016, the UK held a referendum in which electors were asked "*Should the United Kingdom remain a member of the European Union or leave the European Union?*" A majority of votes were cast in favour of leaving the European Union. The referendum vote itself is advisory rather than legally binding on the UK.

Under Article 50 of the Treaty on European Union ("the Lisbon Treaty"), a state may withdraw from the EU "*in accordance with its own constitution.*" In the UK, some parts of this withdrawal process are likely to require some form of parliamentary approval. Once the decision to withdraw from the EU is taken, the Member State is required to formally notify the European Council. In the UK, such notice could theoretically be given by the UK government under the royal prerogative without parliamentary approval. The UK government has stated that the new UK prime minister will have to make the formal notification, which will not be possible before September 2016. However, as discussed above, the ECA 1972 will ultimately need amendment and there may be other parliamentary votes to support the process, e.g. potentially on service of the notice and on any agreement on a new relationship.

Following formal notification, Article 50 confirms that the EU shall negotiate and conclude an agreement with the departing State "*setting out the arrangements for its withdrawal, taking account of the framework for its future relationship with the Union.*" The negotiated terms of the UK's withdrawal agreement with the EU would require the approval of a qualified majority of remaining EU Member States (that is, 20 member states with a combined population in excess of 65% of the total EU population) and the consent of the European Parliament. This withdrawal agreement will also require ratification by the UK parliament.

On one reading of Article 50, the framework for the UK's future relationship with the EU must be agreed concurrently with the withdrawal agreement so that the framework can be '*taken into account*' in the withdrawal agreement. This reading of Article 50 does not seem to have the support of some senior EU officials who have suggested that the timing of any new agreement could be much longer.

The UK would cease to be a member of the EU upon the earlier of the withdrawal agreement being concluded or two years after the Article 50 notification. If the withdrawal agreement is not concluded within two years, the UK's EU membership will lapse. The two year period can be extended, but only with the agreement of all Member States.

Given the uncertainty over the time period required for agreeing the framework for the UK's future relationship with the EU and for agreeing trade deals with non-EU states, it has been suggested that it is in the UK's interest to delay serving the Article 50 notification. However, the UK government will likely want to conclude any negotiations well in advance of the next general election, which is scheduled to occur in 2020.

What Is the Likely Framework for the UK's Future Relationship with the EU?

One 24 June 2016, we published a note discussing potential legal models for any post-Brexit negotiated solution in the context of financial business in particular. You might like to view our note, which is available here. Earlier this year, on 21 March, we also published a note discussing generally the potential legal models for any post-Brexit negotiated solution. This is available here.

Is the Scottish Parliament Able to Prevent the UK Leaving the EU?

The Scotland Act 1998 allows the Scottish Parliament to make laws regarding any matters which are not "reserved matters" for the UK Parliament. These reserved matters include international relations, including relations with the European Union, immigration and the free movement of people. Other obligations that arise under EU law are not reserved to the UK Parliament, but the decision to leave itself would be.

The Scottish Parliament has no powers to legislate regarding the relations between the UK and the European Union. It is for the UK to notify the European Council under Article 50 of the Treaty of the European Union, and for the UK Parliament to ratify the withdrawal agreement regarding the terms of the UK's withdrawal. The Scottish Parliament could clearly make political points by passing motions objecting to steps taken by the UK Parliament or approving certain courses of action (such as a new referendum or other legal changes) if it went ahead, but this would not be legally binding on the UK Parliament.

Will the Scottish Parliament be Required to Implement Any Legislation in Response to the UK Leaving the EU?

The Scottish Parliament would not be required to legislate in order to implement any Brexit decision. The power of the Scottish Parliament to make laws does not affect the power of the Parliament of the United Kingdom to make laws for Scotland. There has been an understanding (now set out in the Scotland Act 2016) that the UK government will not normally legislate on matters which affect Scotland.

The understanding not to legislate on Scottish matters only applies in relation to "devolved" matters, rather than those matters which are reserved (as discussed above). As both the relations with the European Union, and the free movement of persons, are reserved matters, the UK Parliament is able to legislate on these without the approval of the Scottish Parliament. Further, an Act regarding withdrawing the UK from the EU and the future status of EU law in the United Kingdom could hardly be said to be a "normal" piece of legislation. Clearly it is extraordinary and therefore should fall within the powers of the UK Parliament.

Therefore, should the UK Parliament pass an Act confirming the withdrawal, and either in the same Act or in other legislation adopted at the same time repeal the ECA 1972 and stop the direct applicability of EU law within the United Kingdom, it is not immediately transparent that there is anything that the Scottish Parliament can do to prevent this, as a strictly constitutional law matter.

Further, there is no need for any Act of the Scottish Parliament to confirm the UK Act of Parliament amending the ECA 1972. Some arguments have been made that the Scottish Parliament would not be able to pass any legislation repealing EU law because it is outside of the legislative competence of the Scottish Parliament to pass any legislation which is incompatible with EU law. However, as already noted, the UK Parliament retains sovereignty to legislate as regards Scotland. An Act of Parliament repealing EU law within the UK would therefore repeal EU law in Scotland without any need for legislation passed by the Scottish Parliament.

Might EU Law Continue to Have Direct Effect in Scotland Even Though It No Longer Applies in the Rest of the UK?

After a Brexit takes effect, it might be that the Scottish Parliament wishes to continue to apply certain aspects of EU law in Scotland which the rest of the UK does not. If this were the case, then this would be within the powers of the Scottish Parliament as regards devolved matters to, for example, apply EU regulations directly and implement EU directives in a different way to the rest of the UK. However, whilst Scottish judges would have to consider this law, there would be no right for individuals to take cases to the ECJ, as from the EU's

perspective the EU treaties would cease to have effect in Scotland after the expiry of the time period set out in Article 50. Furthermore, this phenomenon would be restricted to the devolved powers, and so would not apply to those powers reserved to the UK government, which includes (amongst other things) the issues of immigration and the free movement of people.

Corporate Law

Overall, we do not expect that the withdrawal of the UK from the EU would have much effect on UK company law but we note below some possible developments.

The UK Companies Act reflects various EU Company Law Directives. Following a withdrawal of the UK from the EU (and unless the UK becomes a member of the EEA), the UK would be free to amend the Companies Act. For example, it may wish to reconsider the requirement for shares to have a par value or to abolish the prohibition on the giving of financial assistance by public companies.

Since 2004, it has been possible to incorporate a European company or Societas Europaea ("SE") under an EU regulation that is directly applicable in the Member States of the EEA. An SE must be registered in one of the member states of the EEA. If, following withdrawal of the UK from the EU, it does not become a member of the EEA, this EU primary legislation will cease to have effect in the UK and the legal status of any registered SE in the UK would, unless provided for in grandfathering provisions, be uncertain at best.

If this uncertainty is not resolved in due course, the limited number of SEs that are registered in the UK may have to consider either converting to a UK public limited company or remaining an SE but changing their registered office to another EEA member state, having taken into account any relevant regulatory, commercial and tax considerations.

Finally, as noted below, the cross border merger provisions of the Companies Act would cease to be available following a withdrawal of the UK from the EU (and unless the UK becomes a member of the EEA).

Trade

How Will the UK Trade with Other Non-EU Countries?

At present, the EU negotiates all external trade agreements with third countries. The UK is unlikely to be able to carry those arrangements across and so will need to negotiate new trade deals with major trading partners. UK politicians have indicated that World Trade Organisation ("WTO") agreements will be the most likely starting point for trade agreements, but the scope of these agreements may not be sufficiently comprehensive and will likely require additional work. This is a major task and it is as yet uncertain how it will be achieved.

How Will the UK Trade with Other EU Countries?

The UK trades with EU countries under the EU treaties. Assuming that the UK leaves the single market, this will no longer be possible and the UK will need to negotiate a new trading arrangement with the EU. There are a variety of models for this. Some give enhanced access to the EU. The UK could rejoin the EEA, if its members, including the EU, permit. Doing so would allow the UK enhanced access to the single market but require keeping free movement of workers, a significant issue in the electorate's decision to leave the EU. Switzerland has its own model which also provides enhanced access—but this also requires keeping free movement of workers. Other countries have free trade agreements which give negotiated access, typically less than those with enhanced status. The UK will have to devise and agree an approach with the EU.

Tax

What are the Implications for Areas of General EU Tax Competency (VAT and Customs Duty)?

Tax is not generally an EU competence, except for VAT and Customs Duty. Given the budgetary importance of VAT receipts, the expectation is that the UK would largely replicate the current VAT system following Brexit. The UK will have flexibility from E-Day to alter rates and the scope of exemptions.

The fact that cross-border supplies of goods and services made (in either direction) between the UK and the remaining Member States will cross into, or out of, the EU following Brexit may well amount to a compliance matter so far as the supply of most business services is concerned. In relation to goods, however, the position on duties and tariffs will depend on the outcome of the forthcoming negotiations on withdrawal, and businesses will need to review the location of their manufacturing and distribution lines. The provisions of long term supply contracts allocating such costs as between the parties will also need to be considered.

What About Other EU Directives (e.g. the Parent/Subsidiary Directive and the Interest and Royalties Directive)?

Currently, certain EU Directives apply in particular circumstances to modify the effect of Member States' internal tax rules. Most notably, the Parent/Subsidiary Directive and the Interest and Royalties Directive limit the scope for domestic withholding taxes to be imposed on certain categories of intra-group payments between the UK and other Member States.

However, the UK has bilateral tax treaties with all of the other Member States, the majority of which have a similar overlapping effect. The application of bilateral tax treaties would not be affected by Brexit.

Therefore, in relation to interest, group structures should only be affected where an intra-group loan falls into one of the gaps in this network of treaty exemptions, for instance when made (in either direction) between the UK and Italy or the UK and Portugal.

In relation to dividends, the UK generally imposes neither corporation tax on intra-group dividends received by a UK company, nor withholding tax on dividends paid by a UK company. Thus the UK tax treatment of dividends would not generally be affected if the Parent/Subsidiary Directive no longer applies. That said, structures will need to be reviewed which currently rely on the Parent/Subsidiary Directive to limit tax that would otherwise be imposed in an EU counterparty country, either: (i) to prevent domestic withholding tax from applying to intra-group dividend payments from an EU subsidiary to a UK parent company absent a full treaty exemption—which could potentially apply to subsidiaries in Austria, Germany, Greece, Italy and Portugal amongst others; or (ii) to exempt a dividend payment by a UK subsidiary from a domestic tax charge in the hands of an EU parent company. Given the extension to UK withholding tax on royalties announced at the Budget, IP holding structures will also need to be considered carefully.

Where the above considerations necessitate a group restructuring, proceeding by way of a cross-border merger can be a helpful technique. Cross-border mergers of UK incorporated companies were not historically recognised under UK domestic law, but have been enabled since 2007 pursuant to the provisions of EU Mergers Directive (associated tax reliefs on a merger were provided by further directives). Other restructuring techniques may be available (such as incorporating new intermediate holding companies, and hiving the existing subsidiaries up or down the group). However, where it is desirable to proceed by way of cross border merger, group restructurings may need to be planned and implemented before Brexit, if the UK company law provisions that currently implement the Mergers Directive cease to apply.

The issue of shares by a UK incorporated company was subject to a 1.5% stamp duty charge in certain specific scenarios, prior to cases brought largely under the EU Capital Duty Directive which determined that the charge was incompatible with EU law. The relevant scenarios included share issues made into a depositary receipt system, such as American Depositary Receipts, or into a clearance service, like Euroclear, Clearstream and DTC, and also the issue of certain bearer instruments. The 1.5% stamp duty charge remains on the UK statute books, and HM Revenue and Customs will be free to apply it once again if equivalents to the current EU rules are not preserved following Brexit.

It is worth noting that the EU Directive on Administrative Cooperation provides for an information exchange system between EU tax authorities, similar to FATCA, in relation to residents of one Member State holding accounts with a financial institution in another Member State. The substance of this should not change in relation to UK financial institutions or UK account holders following Brexit, as the same ground will be covered on a more global basis by the Organisation for Economic Cooperation and Development ("OECD") Common Reporting Standard.

What Will the Impact be on the General Tax Environment in the UK and Europe?

The EU does not generally have standing to legislate in the direct tax arena without the unanimous agreement of all Member States. Nevertheless, elements of the UK and other EU tax systems have been subject to challenge in the ECJ over compatibility with the EU freedoms of establishment and movement of capital, citing differential outcomes between local and other EU residents or activities. In some cases, adverse decisions have led to changes in the relevant UK rules, for instance on loss relief and the controlled foreign companies regime.

Unless the UK agrees to continue to adhere to the relevant EU freedoms in the course of withdrawal negotiations, the UK tax system will no longer be bound by these constraints following Brexit. The absence of the EU state aid rules could also give the UK more flexibility for targeted tax incentive regimes, for instance permitting further relaxation of the conditions around existing investment incentive schemes (Enterprise Investment Schemes and Venture Capital Trusts) and R&D credits.

But the likelihood is that any systematic change to the UK business taxation system following Brexit will be gradual and incremental. The UK has been vocal in its support of global anti-avoidance efforts such as the OECD Base Erosion and Profit Shifting ("BEPS") project, and international influences of this type will no doubt continue to inform the development of the UK tax system. Conversely Brexit, and the consequent removal of the UK's longstanding vociferous objections to further EU tax harmonisation, may allow the EU Commission to gain more traction for pet projects such as the Common Consolidated Corporate Tax Base within the remaining Member States. It is also possible that the project to introduce an EU financial transactions tax ("FTT"), recently reported to be making little headway even amongst the ten Member States still officially on board to apply the tax, may gain impetus.

Private International Law: Governing Law and Enforcement of Judgments and Awards

What Would be the Impact of Brexit on Usage of English Law?

Brexit does not provide any rationale to stop using English law in commercial contracts. English law is often chosen by contracting parties around the world because of its predictability and commerciality. Similarly, English courts are a popular choice amongst non-domestic parties due to their quality, independence and relative efficiency. Some commentators have noted that European legislation is often high-level, giving rise to

ambiguities, and sometimes inadvertently includes ambiguities that are introduced to resolve controversies arising during the legislative and lobbying process. The limited rise of continental European concepts, which potentially add uncertainty and mitigate against freedom of contract such as good faith, has arguably been influenced by European consumer protection regulation. Clearly English contract law may change depending on how the limited corpus of European contract law legislation is applied post-Brexit, but there is no obvious major impact.

What Is the Impact of Brexit on the UK Approach to the Determination of the Law Applicable to Contractual and Non-Contractual Obligations?

The UK courts currently determine the applicable law of contracts according to two EU regulations; the Rome I and Rome II Regulations. Express choices of governing law are given effect and a series of rules determine applicable law where no choice has been made. The treatment of these EU regulations will depend on the approach to grandfathering discussed above. We would expect a very similar regime to prevail in any event. In the case of the law applicable to contractual obligations, the predecessor regime, the Contracts (Applicable Law) Act 1990 contained substantially the same rules as Rome 1. Whilst there are differences between Rome II on the law applicable to non-contractual obligations and the predecessor Private International Law (Miscellaneous Provisions) Act 1995, the widely recognised additional certainty provided by Rome II means that it is unlikely that the changes it brought in will be reversed.

What Is the Impact of Brexit on Jurisdiction and Enforcement of Judgments?

The UK is currently part of European-wide frameworks (in particular the Recast Brussels Regulation and the Lugano Convention) regulating the determination of jurisdiction and ensuring (subject to narrow exceptions) the recognition and enforcement of judgments by the courts of all Member States of the EU and Iceland, Norway and Switzerland. Again, the continuation of these will depend on whatever grandfathering arrangements are put in place in national legislation and how other EU member states approach UK enforcement.

There are a number of possibilities as to how jurisdiction and enforcement of judgments may be regulated once the UK actually withdraws from the EU. Whichever of these becomes the reality, it is not the case that English judgments will not be enforceable in the EU nor that their enforceability (the bases on which they can be refused enforcement or the time/expense of the process) is likely to be substantially compromised. What happens post-Brexit is likely principally to affect how streamlined a process recognition and enforcement will be. One possible outcome is that the UK (as a new EEA/EFTA member or otherwise) may sign up to the Lugano Convention in its own right (as opposed to as an EU Member State as currently). If this happened, the regime would be substantially unchanged. An alternative would be for the UK to negotiate separate arrangements with Member States en bloc or individually. The UK will want to secure, in particular, the preferential treatment that its courts' judgments currently have in the EU. There would doubtless be some interest from Member States in having their judgments similarly treated in the UK.

Outside the existing European regimes, the UK might accede to the Hague Convention on Choice of Court Agreements, to which the EU is already party. Whilst this does not represent a comprehensive solution, the Convention provides a mechanism for the allocation of jurisdiction where parties have agreed exclusive jurisdiction for a contracting state as well as for recognition and enforcement of judgments.

One anticipated consequence of the UK moving outside the European jurisdictional frameworks is that English courts may again make wider use of anti-suit injunctions. The ability of litigants to use this mechanism against parties commencing proceedings in breach of exclusive jurisdiction agreements has been constrained by the

European Court where such proceedings were commenced in a Member State and also in the arbitration sphere.

What Is the Impact of Brexit on the Enforcement of Arbitral Awards?

The UK's withdrawal from the EU would not affect the position regarding the enforcement of international arbitral awards. The UK is a signatory to the New York Convention (given effect by the Arbitration Act 1996) in an individual capacity, along with 150 other states including all EU member states. Therefore, post Brexit, arbitral awards rendered in the UK will be enforceable in EU member states just as they are now and vice versa.

Mergers and Acquisitions

What Is the Impact of Brexit on Public M&A Transactions?

The UK's withdrawal from the EU is not likely to have a material impact on the terms on which public M&A transactions in the UK are regulated or effected.

Public M&A transactions involving UK listed or incorporated companies are governed by the UK Takeover Code. The EU's Takeover Directive was strongly influenced by the UK takeover regime and the UK regime was not materially changed in order to accommodate implementation of the directive. As a result, it is unlikely that any significant changes would be made to the UK's takeover regime as a result of the UK's withdrawal from the EU.

One aspect of the EU Takeover Directive which has been reflected in the UK Takeover Code is that of shared jurisdiction between EU regulators where a target company has its registered office in one Members State and its securities admitted to trading on a regulated market in one or more other Member States. These rules will continue to apply if the UK becomes a member of the EEA. If the UK does not become a member of the EEA, the rules would cease to apply but the Takeover Panel is likely to consider whether it would be appropriate to put in place equivalent measures with other takeover regulators.

What Is the Impact of Brexit on Private M&A Transactions?

The principal effect of withdrawal from the EU on private M&A transactions is likely to be limited, as regards the commercial terms of the transaction. In regulated industries, particularly financial services, or in relation to UK businesses with substantial sales into the EU, the effect of the UK's withdrawal from the EU will need to be factored into the commercial terms of the transactions (e.g., more warranties are likely to be requested, greater comfort regarding the structure of the business will be required, etc.), and will be a focus of due diligence.

In the case of private M&A transactions that are effected by way of transfer of a business or undertaking, since the 1980s UK law has implemented the Acquired Rights Directive and provided that contracts of employment of those employees employed by the transferor and are "*assigned to the organised grouping of resources or employees that is subject to the relevant transfer*" automatically transfer to the transferee on their existing terms, with the exception of certain old age, invalidity and survivors' benefits under occupational pension schemes. The transferee takes on the transferring employees on their existing terms of employment, and can only make changes to their terms in limited circumstances. Although it is possible that the UK may relax certain aspects of this regime following the UK's withdrawal from the EU (the loss of the pan-EU freedom of movement in particular may result in some amendments), it can be expected that this regime will continue to be a feature of UK law.

Since 2007, it has been possible to merge limited liability companies incorporated in different Member States of the EEA. Unless the UK joins the EEA, this regime would not continue to be available following the UK's withdrawal from the EU. In practice, it has not been a feature of many M&A transactions (public or private), although is used quite commonly in intra-group transactions. It is also worth noting that several jurisdictions allow for similar regimes even without the relevant EU directive applying. The UK may decide to implement similar legislation.

How Would Merger Control Rules Change?

Large cross-border mergers are typically dealt with by the European Commission as a one-stop shop. It is likely that such mergers will now also come for review by the Competition and Markets Authority in the UK. This will affect the costs of merger approvals and deal timetables. In addition, EU law currently constrains national governments from intervening in mergers on all but a limited set of grounds other than competition. The UK will be free to create new categories of 'public interest' issues meriting intervention. This issue is discussed further in the Competition section.

Finance

What Impact Could Sterling Volatility Have Under Financing Documentation?

The Brexit vote has caused significant volatility in the financial markets. If this situation continues, borrowers may see an increase in the cost of sterling borrowing, non-UK lenders may have less appetite to lend to UK borrowers and multinational groups may seek to restructure their borrowing arrangements. Although the UK remains subject to EU law and many changes will not occur until Brexit, volatility could have an effect now. Changes in mark-to-market values may have triggered requirements to post more collateral or a need to increase credit lines to obtain more hedging. Financial covenants in financing documentation may be required to be tested shortly by reference to the financial statements for the period ending 30 June. If debt is calculated by reference to the spot rate on 30 June rather than an average rate, or mark-to-market movements are included for derivatives, covenant compliance may be affected. Borrowers may also look to make adjustments to their financial covenants: for example, to reflect future currency movements or to add back to earnings before interest, tax, depreciation and amortisation the costs of contingency planning or reorganisations. Any financial tests based on asset values may also be impacted if asset values have fallen due to market volatility.

Will the Brexit Vote Cause a Material Adverse Effect, Termination Event or Force Majeure Under Financing Documentation?

The specific wording of each financing document must be reviewed. However we would not expect that the vote would trigger a material adverse effect, termination event or force majeure under Loan Market Association ("LMA") standard loan agreements. Material adverse effect is not usually linked to the financial markets but instead to the business of the borrower. In the future, a borrower's business may be affected as a result of the vote or the UK exiting the EU. For example, a business could lose a key licence or authorisation should EU-wide arrangements cease to apply and this could trigger a material adverse change or termination event. This could be a particular risk in highly-regulated industries such as financial services, life sciences, energy and transport if the EU and the UK do not agree to replicate existing arrangements going forward. However it would be highly speculative to make any assessment at present.

Will Brexit Affect Borrowers' Ability to Move Cash Around the Borrower Group to Facilitate Debt Service?

EU provisions which limit withholding tax on certain categories of intra-group payments may cease to apply following Brexit. If the EU and UK do not agree to replicate these arrangements, then withholding tax may become applicable to dividends received by UK holding companies from their subsidiaries in certain EU countries where domestic rules impose withholding on dividends, potentially including Austria, Germany, Greece, Italy and Portugal. Dividends paid by a UK subsidiary could become subject to a tax charge in the hands of an EU parent company, unless a domestic exemption is available in the parent jurisdiction which does not depend on the continuing application of the EU Parent/Subsidiary Directive. Withholding tax may also become applicable to interest on intra-group loans between UK companies and certain EU affiliates, for instance in Italy and Portugal. Where these issues arise, restructuring will need to be considered sooner rather than later, as mergers of UK incorporated subsidiaries may no longer be possible if the cross-border merger procedure under the Mergers Directive ceases to be available following Brexit. Care must be taken when reorganising a group that any requirement for a borrower or guarantor to retain its centre of main interests (HQ) where it is incorporated is not breached or waived. This is discussed further in the Tax section.

Will Provisions in Financing Documents Relating to EU Laws Have the Same Meaning Post Brexit?

Financing agreements should be reviewed to assess whether any terms or definitions referring to EU laws or EU members will need adjustment. For example, loan agreements may permit certain activities (such as acquisitions) to the extent these are in EU member states and such permissions would no longer extend to the UK.

Should EU Borrowers Choose the Law of a Continuing EU Member State to Govern Their Financing Agreements?

Courts in EU member states are required to give effect to the parties' choice of law to govern a loan agreement under the Rome Regulation. Generally, English law provides a strong and stable system for financial contracts which does not suffer from some of the limitations applicable to the laws of continental European jurisdictions. The choice of English law may also facilitate the use of an English scheme of arrangement in restructurings. There may still need to be some changes to the wording of loan agreements to reflect EU laws that may apply and any specific triggers or modifications to apply upon a Brexit. Moving away from English law may carry practical disadvantages. There would be time and costs involved if financing agreements negotiated over several years between lenders and borrowers need to be re-written and a loan agreement would form part of a suite of documentation including documentation to trade the loan which would usually be governed by the same law.

Should EU Borrowers Continue to Choose English Courts to Determine Disputes?

As discussed in the section on Private International Law, the UK currently benefits from the Recast Brussels Regulation and Lugano Convention, which provide common jurisdictional rules under which the courts of the EU and Iceland, Norway and Switzerland recognise the parties' choice of jurisdiction. These rules also provide a framework for the decisions of a court in such a country to be recognised and enforced by the courts of the others. There are a number of possible scenarios that may see the UK largely preserve these arrangements on exit (discussed in the section on Private International Law), but if no substitute treaties are agreed, enforcement of a judgment of an English court in an EU member state would depend on that state's local laws. However, this is no worse than the position that applies to the enforcement of a judgment of a New York court on a financing

agreement in the court of an EU country. Many financing agreements and almost all high yield bond documents contain New York law governing law and jurisdiction clauses. Although enforcement of a New York judgment could take longer and be somewhat more expensive than enforcement of a judgment of a court in the EU due to the lack of any reciprocity arrangements this has not been seen as an issue up to now. Whilst in general we `expect parties to continue to use English jurisdiction clauses for financing agreements, if there is a particular concern around enforcement then local law advice should always be taken on the specific enforcement risk and the choice of jurisdiction. Depending on the final arrangements that the UK and the EU agree there may also be some advantages in selecting an exclusive jurisdiction clause. Parties may also consider arbitration as an alternative, although arbitration is typically not used for loan agreements save in emerging markets transactions. The enforceability of arbitral awards is unaffected by a Brexit as the UK is a party in its own right to the New York Convention which governs the enforcement of arbitral awards in approximately 150 states.

Will Borrowers Continue to Be Able to Borrow From Their Relationship Banks in London?

At present, corporate loans to companies in the UK and some other EU members states can be made by entities without a banking licence, such as funds. Any loss of EU passporting under relevant banking directives would not of itself affect these loans.

Following a full Brexit, non-EU lenders, which have been lending from London to an EU borrower under EU passporting arrangements, may no longer be able to do so under such arrangements. However, banks will be able to continue to lend to corporate clients in member states where that is unregulated without an EU passport, or may do so subject to any new passporting arrangements which could be adopted. In some states other arrangements are possible.

Alternatively, depending on the relevant financing documentation, such lenders may be required to try to lend through a facility office in the EU or transfer the debt to another lender. Failing that, the borrower may be required to repay the affected lenders if the lending would otherwise become illegal and no applicable grandfathering provisions for outstanding liabilities is agreed. Parties to lending agreements may wish to build in some flexibility to negotiate a restructuring of lending arrangements which could become unlawful before a loan becomes repayable.

Will Schemes of Arrangement Be Affected by Brexit?

The UK and other EU member states (other than Denmark) are subject to the European Insolvency Regulation. The Regulation provides a framework for mutual recognition of insolvency proceedings. However the Regulation imposes some restrictions on where insolvency proceedings can be commenced. Main insolvency proceedings, such as an English administration, can generally only be opened where a debtor has its centre of main interests (HQ). The Regulation, and the Recast Regulation which will apply from June 2017, will cease to apply from a Brexit. The UK could well seek to negotiate an alternative agreement for recognising and enforcing insolvency proceedings with EU member states.

A scheme of arrangement is not treated as an insolvency proceeding for the purposes of the Regulation and is not subject to its jurisdictional restrictions. A foreign company can commence proceedings for a scheme in the English courts if it can establish “sufficient connection” to England and Wales, for example, by having debt documentation containing an English governing law and jurisdiction clause. However schemes are not automatically recognised in another EU member state, so an English court will need to be satisfied that the scheme will be recognised in the debtor’s member state under its local law. This position should not be affected

by Brexit and is a good reason why borrowers may wish to continue to use English law loan agreements. Many EU member states have revised their national insolvency procedures in recent years following the financial crisis and the revisions have resulted in viable alternatives to English schemes.

The UK and a small group of other countries, mostly outside the EU, are party to the UNCITRAL Model Law on Cross Border Insolvency. This provides for mutual recognition of insolvency proceedings, including English schemes, on a more limited basis than the Regulation. This will also be unaffected by Brexit.

What About the Bank Recovery and Resolution Directive (BRRD) Regime?

The BRRD provides for a system of mutual recognition of bank recovery steps taken by authorities in Europe, such as write-down of creditors, bail-in, and splitting of a good bank/bad bank. The aim is for such steps to be supported throughout Europe, so as to reduce legal uncertainties and reduce the likelihood of taxpayer money being used to finance the banking sector in times of economic stress. Many UK banks have EU branches and many EU banks have UK branches. It may therefore be important for EU recovery and resolution steps to be recognized in the UK, and for UK recovery and resolution steps to be recognized in the EU. The outcome of any discussions on this topic may depend on how the passporting of financial institutions, discussed in our separate note referred to above (which is available here), is resolved, and on how the UK government approaches grandfathering issues. We would anticipate some form of mutual recognition regime being put in place.

Will We Need Bail-In Clauses in English Law Agreements?

Another requirement of the BRRD is for so-called “bail in clauses” to be included in contracts entered into by EU based banks but governed by a non-EU law. Such clauses include a contractual agreement to, and recognition of, the validity of steps taken by governments under the BRRD. If there is no cooperation to resolve the recognition issue (discussed in the above paragraph), then we may end up in a situation where all English law agreements would have to include EU “bail-in language.” This could present a major logistical challenge for European markets and legal advisers, given the importance and widespread usage of English law in agreements by EU-based banks. We would anticipate some form of mutual recognition regime being put in place.

What Impact Does Brexit Have on Derivatives Transactions?

London is a global centre for derivatives trading. Many derivative transactions entered into around the world are governed by English law or entered into with banks and other financial institutions established in the UK, even if governed by New York law. A significant proportion of the legal and regulatory regime relevant to derivative transactions traded in London is derived from EU directives and regulations.

The vote in favour of Brexit has not, of itself, changed the law in the UK, or the applicability of any EU laws relevant to derivatives trading in the UK. The vote should therefore not have had any direct effect on, or triggered any contractual or other legal consequences under, a standard International Swaps and Derivatives Association (“ISDA”) Master Agreement. The Article 50 notification would similarly not, of itself, have any direct effect on, or trigger any consequences under, a standard ISDA Master Agreement.

When the UK does cease to be a member of the EU, it is possible that there may be significant legal and regulatory changes relevant to derivatives transactions. Issues relevant to derivatives that may be impacted by the UK ceasing, in due course, to be a member of the EU include:

- Bank resolution including the Bank Resolution and Recovery Directive;

- Insolvency including the EU directives on the reorganisation and winding up of Credit Institutions and Insurance undertakings;
- Clearing and related obligations under the European Market Infrastructure Regulation ("EMIR");
- Regulatory capital including the Capital Requirements Regulation;
- The Markets in Financial Instruments Directive ("MiFID");
- Collateral arrangements including the EU Collateral Directive;
- Governing law and dispute resolution provisions.

The extent to which these or any other EU derived laws and regulations will continue to apply in the UK after Brexit will depend upon the exit model adopted and the availability of "equivalence"-based third country access, discussed in our note dated 24 June (which is available here). It is likely that the UK would elect to continue to apply the vast majority of EU based financial services laws and regulations even if not technically obliged to do so.

The precise terms upon which the UK would leave, its post departure arrangements with the EU and any resulting changes in the law need to be established and are impossible to predict precisely at this stage. As a result, it is not possible at this stage to determine what changes will need to be made to documentation in the future. Generally speaking, however, we do not anticipate many changes will be necessary to derivatives documentation.

Capital Markets

What is the Impact of Brexit on UK Issuers' Ability to Make Public Offers of Securities in the EU?

Currently, most non-EU companies accessing capital markets in the EU do so on an exempt basis. For those that do not, primary capital markets activity is governed by the EU's Prospectus Directive. This allows issuers to choose a "home member state" which is responsible for the approval of offering and listing documentation. Approval of that home member state allows the issuer to apply for a "passport," under which an offering may be made into other member states, using the same prospectus, subject only to minor additional requirements. The EU's Transparency Directive and soon-to-be in force Market Abuse Regulation govern disclosure issues for capital markets. The Transparency Directive also provides for the election of a "home member state" in the EU, which is responsible for receiving disclosures, such as updated accounts, new annual and other periodic reports and significant shareholding notifications. For EU-based issuers, the home member state is their member state of corporate incorporation. For non-EU-based issuers, it is the place in which they first make an offer or apply for a listing. It is also possible for an issuer (often based in a smaller EU jurisdiction) to use the Prospectus Directive passport to get a secondary listing on a larger EU market with greater liquidity, such as London.

The main potential impact of Brexit would be for UK-listed companies, whether domestic or non-EU, who wish to engage in retail offers of securities outside the UK, who face the need for a further review of relevant prospectuses by an EU "home member state" supervisor. We expect the UK to continue to make the secondary listing process straightforward.

The European Securities and Markets Authority ("ESMA") is the EU authority tasked with safeguarding the stability of the EU's financial system by enhancing the protection of investors and promoting stable and orderly

financial markets. ESMA has adopted a framework under which a third country issuer that has drawn up a prospectus in accordance with its home country's legislation can meet the requirements of the Prospectus Directive. If the UK does not become a member of the EEA, or of something newly developed with similar effect, following its withdrawal from the EU, UK issuers would be able to make use of this mechanism.

First, ESMA would need to assess the UK's prospectus regime and publish an opinion setting out the list of additional items which would have to be included in a wrap to a UK prospectus to meet the requirements of the Prospectus Directive. As the UK's current prospectus regime is derived from the Prospectus Directive, then assuming that the grandfathering approach discussed in the section regarding the applicability of EU law is adopted for existing EU legislation, it is to be expected that no additional information would be required by ESMA.

Issuers from the UK would then be able to apply to the competent authority in their 'home' Member State (i.e. the non-UK Member State in which the securities are first offered to the public or admitted to trading) to make use of the arrangement. The application would need to include a written confirmation from the issuer that the prospectus has been drawn up in accordance with UK law.

The competent authority in the home Member State will examine the prospectus and the wrap. If satisfied that the requirements are met, it can approve the prospectus and wrap together as a prospectus under the Prospectus Directive. The prospectus may then be passported into other Member States. Effectively, a UK listed issuer would need a second prospectus approval, as things currently stand, in order to sell the securities to European retail investors. It should be noted however that no such prospectus is needed for offers to so-called "qualified investors" and that it is possible that any post-Brexit deal may address this situation.

Should Public Companies Change Their Disclosures in Light of the Brexit Vote?

In light of the economic and political impact of the Brexit vote, both on the UK and the EU, securities regulators will be focused on how companies evaluate and discuss the any potential material impact on their business. Public companies should evaluate the potential fallout from the Brexit vote and consider including in their risk factors and forward looking statements. It is advisable to consider including a general risk about the impact of the Brexit vote on economic conditions or more specific risks about how a potential withdrawal of the UK from the EU and any follow on effects might impact business in the UK and the EU. Set forth below is a general risk factor that public companies can consider as a starting point, as well as examples of business specific risk factors:

> "*In a non-binding referendum on the United Kingdom's membership in the European Union in June 2016, a majority of those who voted approved the United Kingdom's withdrawal from the European Union. Any withdrawal by the United Kingdom from the European Union ("Brexit") would occur after, or possible concurrently with, a process of negotiation regarding the future terms of the United Kingdom's relationship with the European Union, which could result in the United Kingdom losing access to certain aspects of the single EU market and the global trade deals negotiated by the European Union on behalf of its members. The Brexit vote and the perceptions as to the impact of the withdrawal of the United Kingdom may adversely affect business activity, political stability and economic conditions in the United Kingdom, the Eurozone, the European Union and elsewhere. The economic outlook could be further adversely affected by (i) the risk that one or more other European Union countries could come under increasing pressure to leave the European Union, (ii) the risk of a greater demand for independence by Scottish nationalists or for unification in Ireland, or (iii) the risk that the euro as the single currency of*

the Eurozone could cease to exist. Any of these developments, or the perception that any of these developments are likely to occur, could have a material adverse effect on economic growth or business activity in the United Kingdom, the Eurozone, or the European Union, and could result in the relocation of businesses, cause business interruptions, lead to economic recession or depression, and impact the stability of the financial markets, availability of credit, political systems or financial institutions and the financial and monetary system. [Given that we conduct [a substantial portion] of our business in the European Union and the United Kingdom, any of these developments could have a material adverse effect on our business, financial position, liquidity and results of operations.]

[*New or modified trading arrangements between the United Kingdom and other countries may have a material adverse effect on our [export volumes][margins][and may cause us to relocate operations and incur the expenses of such relocations*.]]

[*A decline in trade could also affect the attractiveness of the United Kingdom as a global investment centre and, as a result, could have a detrimental impact on the level of investment in companies with operations in the UK or which service the UK market, including our business, and ultimately on UK economic growth.*]

[*The uncertainty concerning the timing and terms of the exit could also have a negative impact on the growth of the [UK][European Union] economy and cause greater volatility in the [pound sterling][euro][other EU currencies].*]

[*Changes to UK border and immigration policy could likewise occur as a result of Brexit, affecting our ability to recruit and retain employees from outside the United Kingdom.*]"

Should We Expect Significant Changes in Documentation Relating to Equity and Debt Offerings Due to the Brexit Vote?

We do not expect significant changes in documentation relating to equity or debt offerings, such as representations and warranties in purchase agreements. We do however expect to see underwriters adding questions concerning the impact of the Brexit vote on issuers to their due diligence questionnaires and expect them to conduct due diligence on the completeness of Brexit related risk factors, particularly for companies with significant business in the UK or the Eurozone.

Can We Talk to Key Securities Analysts About the Impact of Brexit on Our Business?

Getting ahead of analysts' questions about the impact of the Brexit vote may make sense for companies with operations in the UK or Eurozone. Companies that wish to do so should be mindful of avoiding selective disclosure and should evaluate whether any part of the proposed discussion could be considered material non-public information. If so, they should consider issuing a press release or current report so that the information is broadly disseminated to comply with the applicable disclosure rules (including Regulation FD, if applicable) and as a best practice. Some issuers who might be thought of as most severely affected may wish to consider making additional public disclosure about their contingency plans.

How Does Brexit Impact Considerations for Choosing a European Securities Regulator? If We Have Chosen the UK as Our Primary Regulator, Can and Should We Make a Change?

Many non-EU issuers have not had to choose an EU home country regulator and would be advised to maintain that flexibility. This is because these companies almost always issue securities above the minimum threshold which requires the issuer to make a binding selection of an EU home country regulator.

Going forward and assuming that the UK is outside the EEA or a similar regime, it's possible that companies that had chosen the UK as their primary regulator would be in the same position as other issuers accessing the EU market for the first time (i.e., they would need to elect a new home member state). We would advise such issuers to avoid making a binding home country regulator selection unless it is necessary, until the UK's relationship with the EU has been clarified.

Financial Services

Will It Be Possible to "Passport" UK Based Financial Institutions Into Other EU Jurisdictions?

This is addressed in our separate note dated 24 June, which is available here.

What Impact Will There Likely Be for UK-Based Credit Rating Agencies?

The EU Regulations on Credit Rating Agencies ("CRA") has a third country regime allowing recognition of credit ratings for certain regulatory purposes where the rating is: (i) issued by a non-EU CRA from a jurisdiction with laws approved by ESMA to be "as stringent" as EU laws and endorsed by an ESMA-registered CRA; or (ii) are issued by a non-EU CRA from a jurisdiction with laws that have been deemed by the European Commission as "equivalent" with the EU Regulations on CRAs. Equivalence would be likely given that the UK has currently implemented all EU CRA regulation.

Will the UK Anti-Money Laundering (AML) Regime Be Affected?

The UK has implemented the EU's Money Laundering Directives, so the short answer is that the general analysis above on the European Communities Act and grandfathering will apply. The UK has also "gold plated" EU requirements applicable under EU legislation on AML. For example, the UK has adopted an "all crimes" approach to AML regulation in which there is no *de minimis* level of predicate offence below which offences do not need to be reported. It also has a bespoke reporting and clearance regime for the regulated sector involving the National Crime Agency, not replicated elsewhere in Europe. The UK will also remain a member of the Financial Action Task Force ("FATF"), which established an international AML framework applicable to all FATF members. We would not expect any material changes to the overall regime.

Funds

What Impact Does Brexit Have on UK Fund Managers?

The UK (and London in particular) is home to a large number of fund managers. Those managers may manage alternative investment funds (hedge, private equity, real estate, etc.), in which case they are currently subject to the Alternative Investment Fund Managers Directive ("AIFMD"). Alternatively, they may manage Undertakings for Collective Investment in Transferable Securities ("UCITS") funds, an activity which is currently covered by the UCITS Directive. Finally, managers may act as sub-managers under delegation, or manage individual accounts or other arrangements that are not covered by AIFMD or the UCITS Directive (in which case, they are currently subject to MiFID, as discussed in our separate note dated 24 June, which is available here).

Until the time of withdrawal, the prevailing European laws described above of course continue in full force and effect. At this early stage, managers would be well-advised not to take any knee-jerk business decisions to move operations to another EU member state, given that the existing regime includes various possibilities for third country firms, as discussed in our separate client note. Instead, those managers should monitor developments during the transitional period during which the UK's withdrawal is negotiated.

How Does Brexit Affect UK Managers of Non-EU Alternative Funds?

Many UK managers' funds are based outside of the EU, including in offshore jurisdictions such as the Cayman Islands, the British Virgin Islands, Bermuda or the Channel Islands. For those managers, the AIFMD currently brings with it plenty of regulatory burden, without the benefit of the marketing or management passports.

Once the UK has left the EU, assuming no special deal or status is negotiated, a UK manager would be treated under the AIFMD as a non-EU manager, much like managers domiciled in the United States, Singapore or Hong Kong. The AIFMD would therefore apply to UK managers only where the UK manager wished to market its funds to EU investors, in that marketing would be restricted. However, UK managers are currently restricted in the marketing of non-EU funds to EU investors in a way that is almost identical already. So from a practical perspective, a Brexit would be unlikely to significantly impact on EU managers in this respect. Indeed, the UK would be free if it wished to repeal the AIFMD (as implemented in the UK) and, in doing so, remove some of the regulatory burden affecting UK fund managers.

However, UK managers currently enjoy the benefits of access to the single market for other relevant reasons (such as trading). The implications of a Brexit on such access are discussed in our separate note (available here).

How Does Brexit Affect UK Managers of EU Alternative Investment Funds?

As well as being subject to the regulatory burden of the AIFMD, managers of EU funds are able to enjoy the principal benefits of the AIFMD: marketing and management passports. Those passports, if triggered, allow UK managers to manage funds domiciled elsewhere in the EU and to market EU-domiciled funds to professional clients across the EU.

Were the UK to be treated like other non-EU managers post-withdrawal, UK managers would, in the absence of a negotiated special deal or status, lose their rights to such passports.

The Management Passport

Non-EU managers are, subject to local law in the EU country of domicile of a fund, able to manage EU alternative investment funds. Removal of the passport therefore would not, in and of itself, necessarily create issues for UK managers. However, the AIFMD does contemplate extension of the marketing and management passports to non-EU managers. Were the passports to be extended to UK managers (see below), then it is expected that UK managers would at that stage have no option but to manage their EU funds on the basis of the passport regime. That is discussed further under "Extension of the Passports" below.

The Marketing Passport

Were UK managers to lose rights to the marketing passport, they would no longer be able to market freely to professional clients in the EU. Instead, UK managers would have to operate under private placement exemptions, just like other non-EU managers today, unless and until the passport was extended to the UK as a whole (see below under "Extension of the Passports"). Even then, once UK managers benefit from the marketing passport, it is currently expected that there will be a period of several years during which a UK manager could elect not to market using the passport, and instead market under private placement regimes.

Extension of the Passports

The AIFMD contemplates the possibility that passports will be extended to non-EU managers and funds at some point. The procedure is broadly that ESMA has to assess a country against various barometers, including

in relation to systemic risk and investor protection. ESMA is then tasked with providing written advice to the Commission, recommending (or otherwise) the extension of the passports to the relevant countries. At the time of writing, the passports have not been extended to any non-EU country, although favourable reports have been given in respect of, for example, the Channel Islands.

It seems improbable that the UK, at least if it retains all or most of the AIFMD as implemented in the UK, would not pass the tests necessary for an ESMA recommendation. The timing of the extension of the passports to the UK is less certain, given how glacial the process has been to date in respect of other non-EU countries. Yet it appears that extension of the passports should in reality be something of a formality.

If the passports are extended to the UK, then UK managers would be in much the same position as they are in now, except that managers operating under the passports would be expected to submit themselves to regulation by a regulator in their "Member State of Reference." In practice, while the rules which apply to a UK manager substantively would be unchanged from now, a UK manager would find itself notionally subject to regulation by (for example) the Central Bank of Ireland, as well as by the FCA.

The AIFMD is due to undergo a full review starting in 2017.

How Does Brexit Affect UK Managers of UCITS?

UK managers may manage UK or other EU UCITS funds. There is currently no ability for a non-EU manager to be the management company of a UCITS (since the management company must be domiciled in the EU). In the absence of a negotiated special deal or status, UK funds will cease to be governed by the UCITS Directive and would presumably need to lose the "UCITS" label. They will not be capable of being marketed across the EU under the UCITS Directive and would instead be treated for that purpose as alternative investment funds subject to the AIFMD (see above). We note that the majority of UK UCITS funds currently are marketed either exclusively, or in the majority, in the UK and not in other EU member states, with the result that the consequences of a Brexit will be significantly lessened for such funds.

UK management companies of UCITS domiciled in other EU member states will not be able to continue in that role, in the absence of a negotiated special deal or status. However, such managers could consider re-structuring themselves as sub-managers, operating under delegation from another EU management company, in order to continue to effectively manage such funds.

What Are the Implications for Non-UK Managers?

Marketing of non-UK UCITS funds to UK investors could conceivably be restricted following withdrawal, assuming that the marketing passport is no longer available to be used for marketing to UK investors. It is possible, however, that the UK regime would treat such other UCITS funds as recognised schemes (or similar) under the UK regulatory framework in order to allow continued marketing.

Similarly, marketing of non-UK alternative funds under the AIFMD marketing passport (where available; i.e., currently only for EU managers of EU funds) could be restricted. For non-EU managers, who currently have no access to the marketing passport and thus have to operate under private placement, little is likely to change; private placement will continue to apply. Indeed, if the AIFMD, as implemented in the UK, were to be repealed in a post-withdrawal UK, then non-EU managers could potentially avoid the reporting and other transparency-related burden they currently face.

For non-EU managers of UK-domiciled funds, the AIFMD currently contemplates that (once the passport is extended to such managers) those managers would have no option but to become regulated under the AIFMD. If the AIFMD were repealed post-withdrawal, this requirement, which has yet to be imposed because the passport has yet to be extended, could fall away.

What Will Happen to the Capital Markets Union?

The EU is embarking on a set of changes to laws relevant to capital markets, so as to stimulate more investment in the single market and capital raisings by small and medium sized enterprises. This will likely include amendments to the prospectus directive as well as new legislation. Those laws which come into force before Brexit takes effect will probably be grandfathered, as discussed above. For new directives and regulations, we expect the UK to review these and implement as it sees fit.

Financial Sanctions

How Will Financial Sanctions Be Affected?

The Brexit vote has led to significant uncertainty as regards the future of UK sanctions policy. There are indications that UK sanctions prohibitions will become stricter than current EU legislative processes generally allow.

The House of Commons Foreign Affairs Committee published a report earlier this year on the implications of the referendum on EU membership for the UK's role in the world which noted that the UK is "one of the most influential players in driving EU foreign policy." The report also noted that following a Brexit, the UK would have to "re-assess its sanctions regimes…as it would no longer be bound by the EU's collective rules."

United Nations sanctions would continue to be implemented in the UK. However, the UK would be able to publish sanctions autonomously as regards the scope of UN sanctions, as well as any other measures it wishes to implement. The UK could follow Switzerland's general approach by publishing rules which are similar to EU legislative measures. However, it is more likely that the UK would increase its sanctions powers. It is quite possible that there would frequently be close alignment with sanctions published by the US Office of Foreign Assets Control ("OFAC"), which are generally stricter than EU measures.

Questions also exist as to whether the UK would adopt a modified financial sanctions framework in the British Overseas Territories. The UK has generally refused to accept the automatic extension of EU regulations to the Overseas Territories unless explicitly extended by the UK Privy Council (frequently many months later, and sometimes in different language).

Stricter UK sanctions rules could be implemented in the context of a more aggressive enforcement environment. Parliament is currently discussing draft legislation to give to the new UK sanctions agency (the Office of Foreign Sanctions Implementation) more robust powers. These proposed powers include fines on a civil basis, deferred prosecution agreements, serious crime prevention orders, and longer imprisonment terms.

Competition and Procurement Law

How Would Post-Brexit Competition Law Apply?

The UK, like most other Member States, has its own competition law regime. The substantive rules in the UK largely mirror those in the EU and are considered to work well. No change in the substantive rules around restrictive agreements, abuse of dominance, cartels or merger control is expected.

If the UK were to leave the single market, the UK would regain jurisdiction over deals that would previously have been notified to Brussels for the whole of the EEA. This is unlikely to make any difference to the vast majority of deals since the UK has a voluntary system of merger notification (i.e. clearance is not required before closing); and the UK agency in common with most agencies in the world would most likely follow the EU and US in major deals. An exception may be deals that have a strong nexus to the UK—but, even here, the substantive outcomes are likely to be consistent with the EU and US.

In antitrust, were the UK to leave the single market it would regain jurisdiction over cases that are currently opened by the Commission for the whole of the EU. Theoretically, this allows it to undertake more "me too" type cartel infringement decisions, for example against banks. However, the UK agency is careful with its resources and has a disappointing record of under-enforcement in the UK domestic economy. It is unlikely to consider doubling up with the Commission an effective use of resources.

Would State Aid Rules Change?

State aid is an area of potentially more significant change. Were the UK to retain access to the single market, it is likely that the Commission would also retain State aid control over the UK. If State aid control were to be avoided, it would afford the UK significant additional freedom to implement a more assertive industrial policy via the tax system, public contracts and grants. The only remaining external constraint would be the WTO Subsidy and Countervailing Measures Agreement, although this only prohibits export subsidies and subsidies requiring the use of domestic products. Other subsidies are permitted unless another WTO member can prove harm to their domestic industry. This is far less intrusive than the EU State aid rules, which require subsidies and other Governmental assistance to industry or regions to be approved *ex ante* by the Commission.

How Will Ongoing Cases Be Affected?

All current antitrust and State aid cases currently before the Commission concerning the UK are likely to be heavily deprioritized. In practice, the Commission's ability to enforce its decisions (particularly in State aid) against the UK rely heavily on Member State cooperation, which it can no longer be sure of receiving.

How Will Regulations Governing Public Procurement Change?

The regulations governing public procurement in the UK implement certain EU directives. Should the UK leave the single market, it could choose to repeal these requirements.

EU public procurement rules organise the way public authorities and certain public utility operators purchase goods, works and services. The rules, among other things, require the publication of certain public tenders, adherence to certain pre-defined procurement procedures and prohibit discrimination against a tendering business because it is registered in another EU country.

Even if these rules are no longer applicable, the UK will be still be subject to the Government Procurement Agreement ("GPA"), a WTO Agreement. The GPA requires, among other things, guarantees of national treatment and non-discrimination and detailed procurement procedures. The GPA is subject to the WTO dispute settlement procedure.

In practice it is unlikely that there would be considerable changes to the UK's procurement rules, particularly taking into account domestic UK obligations on public authorities to provide "best value" when procuring goods and services, as well as domestic anti-bribery, anti-corruption and competition laws. The current procurement framework is generally considered to serve these objectives well.

Privacy and Data Protection

What Effect Would Brexit Have on Privacy and Data Protection?

Privacy rights for individuals in Europe are governed in part by the EU's Data Protection Directive. This will be replaced in due course by the General Data Protection Regulation framework starting in 2018, before the likely date of any Brexit. The intent of the GDPR was to provide further harmonisation and uniformity across Europe. There is also a patchwork of national bank secrecy and confidentiality laws in place, which has not been harmonized and should not be affected by the Brexit situation.

Pending E-Day, the current data protection regime in the UK remains intact and UK businesses should continue to comply with the EU regime, including the General Data Protection Regulations ("GDPR") in due course. As for other legal areas, what happens next will depend on the grandfathering provisions.

A particular cross-border issue under the current data protection regime is that any transfers of personal data to outside the EEA can only take place under certain specific conditions. It remains to be seen whether Brexit will also result in exit from the EEA.

Assuming that the UK leaves the EEA, the potential routes for exporting personal data from the EEA to the UK are: (i) with the consent of the data subject; (ii) entering into "model agreements" (in the format published in a Commission Decision) between the UK and EU legal entities; (iii) "binding corporate rules" (which are little-used, but may work in some corporate group contexts); or (iv) a declaration of a safe harbour for transfers to the UK. The latter may be possible if the UK keeps harmonised laws in this area. If the UK adopts its own data protection legislation following the EU model and imposes restrictions on transfers to outside the UK, then all the same issues would need to be explored in reverse.

As the UK Information Commission's Officer ("ICO") cautioned on Friday, "The Data Protection Act remains the law of the land irrespective of the referendum result. If the UK is not part of the EU, then upcoming EU reforms to data protection law would not directly apply to the UK. But if the UK wants to trade with the EU on equal terms we would have to prove "adequacy" of the UK data protection regime." In any scenario, if the UK's data protection standards differ materially from those of the EU, then serious difficulties would be created for both UK and European businesses.

What Are the Data Protection Implications for US Companies?

It is important to note that the GDPR will be applicable regardless of whether the company is in the EU. What triggers the applicability of the GDPR is who the data is about, not where the data resides. So long as the US-based business processes information about individuals in the EU, the GDPR will apply. The United States multinationals and tech firms continue to be in a state of uncertainty as the US Safe Harbor program was declared invalid and its replacement, the EU-US Privacy Shield, while finalised, still needs to be formally adopted. This is because the EU had not so far given an "adequacy" decision that would declare the US safe as a destination for Europeans' personal data. Recent enforcement cases in Germany suggest that an attempt to use the "model clauses" is prudent for the time being, until the Privacy Shield is in place, although the validity of the model clauses approach has also been referred recently to the European Court. Brexit should not have any immediate impact on these existing issues.

Intellectual Property

What Impact Will Brexit Have on Intellectual Property?

The UK's decision to leave the EU will have consequences for the protection of intellectual property. A major focus of the EU over the years has been to harmonize intellectual property laws among its member states. If the UK ceases to be treated as part of the EU, then certain measures taken by the EU to harmonize intellectual property laws may in time change, resulting in potential inconsistency. The outcome will depend on how EU legislation is grandfathered, as discussed above.

It bears mentioning that certain types of intellectual property rights will be more affected by Brexit than others. The types of intellectual property rights that are expected to be most directly affected are the ones created and recognized to exist on an EU-wide basis, such as Community Trade Marks, Community Designs and Community Plant Variety Rights. The existence of these intellectual property rights in EU member states is correlated to EU membership. Once Brexit occurs, unless something specific is done in UK legislation, these intellectual property rights will no longer be recognised in the UK.

Unlike the Community rights mentioned above, there does not appear to be any significant effect of Brexit on existing patent rights. The European Patent Organization is independent of the EU, so it is unlikely that Brexit will affect the UK's ability to continue functioning as a member state of this organization. Furthermore, it does not appear that Brexit will affect the UK's ability to continue to participate in the Patent Cooperation Treaty and the Paris Convention.

While Brexit will have minimal adverse impact on existing patent rights, it is expected to have a larger impact on the prospective unitary patent regime that the EU has been negotiating with its member states. For years, the EU has been working on creating pan-European patent protection via a single patent, known as the Unified Patent. Once Brexit occurs, the UK is not expected to be able to participate in the new Unified Patent system, as such system will only be available to EU member states.

What Steps Can Be Taken to Minimize the Impact of Brexit on Intellectual Property?

The UK Government will need to review intellectual property laws that derive from EU laws to ensure that they can still validly operate within the UK after Brexit. To the extent that such laws do not apply within the UK after Brexit, separate legislation may be necessary to recreate such laws in the UK.

The UK Government should also work with the EU prior to Brexit to create UK-specific transitional and/or replacement rights so that the people who own and rely on Community rights do not automatically lose the UK territorial protection of their Community rights upon Brexit. The UK Government might consider establishing and benefiting from the Unified Patent system that is currently in development by the EU. Similar to the case with Community rights, the UK Government should work with the EU prior to Brexit to create some means of supplemental protection to the Unified Patent that covers the UK.

While creating UK-specific intellectual property rights to cover the gaps in Community rights and Unified Patent rights left in the wake of Brexit will fall to the UK Government, granting these rights will likely fall to the UK Intellectual Property Office ("UKIPO"). This can be reasonably expected to not only increase the administrative burden of the UKIPO, but also increase the filing costs for people that place importance on owning such intellectual property rights in the UK.

Human Rights Laws

The European Court of Human Rights, which applies and interprets the European Convention of Human Rights ("ECHR"), will still have jurisdiction over UK human rights issues. The ECHR framework is established under a different European arrangement (the Council of Europe, which has 47 member states, including Russia) and is implemented in the UK through different national legislation (the Human Rights Act 1998, not the ECA). However the ECHR has also been recognised as a general principle of EU law, meaning that the Court of Justice may use ECHR decisions as a legal source in deciding EU cases.

There have been proposals, at a political level, for the UK to exit the ECHR and replace it with a UK bill of rights, notably in the Conservative party's manifesto in the last general election. At the EU level, even though the Treaty of Lisbon obliges the EU as a whole (distinct from its constituent member states) to sign up to the ECHR (which would make decisions made by EU institutions justiciable under the ECHR) in 2014 the EU Court of Justice issued an opinion rejecting a draft accession agreement as incompatible with EU law.

The EU has its own Charter of Fundamental Rights of the European Union, although the recitals to this, and a protocol secured by the UK, clarify that this Charter is not intended to increase the scope of EU laws or create any additional rights but merely consolidates pre-existing rights under EU law.

It therefore remains to be seen whether: (i) the UK's withdrawal from the EU will lead to its related protocol on the application of the Charter being withdrawn; (ii) the EU Court of Justice will seize upon these circumstances to extend the scope of the Charter; (iii) the Conservative party will implement their manifesto pledge to replace the ECHR at the UK level; (iv) the EU will accede to the ECHR; or (v) Single Market negotiations between the UK and the EU will include provisions relating to either the Charter, the ECHR as a general principle of EU law, or the ECHR by virtue of the EU acceding to the ECHR, in each case irrespective of any UK effort to remove UK law from the ECHR or the Charter.

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