
August 29, 2018

Risk of a “no deal” Brexit: How should businesses respond?

With exactly seven months remaining until the United Kingdom is scheduled to withdraw from the European Union, its negotiations with the EU on the terms of its withdrawal and its future relationship are, in the words of Prime Minister Theresa May,¹

at an impasse. The two options on offer from the EU at the moment are not acceptable to me, or to the United Kingdom.

As described by May, the first of these options is a free trade agreement for Great Britain, with Northern Ireland staying in the customs union and parts of the single market. This approach would solve the challenge presented by the border between the Republic of Ireland and Northern Ireland, allowing the present completely open border between the Republic and the UK – one of the foundational principles of the so-called Good Friday Agreement that largely resolved the “Troubles” that plagued Northern Ireland for over 30 years – to remain as it is. That option would also be fundamentally unacceptable to the Democratic Unionist Party of Northern Ireland (DUP), whose 10 votes the Conservative Party needs to remain in power.

The second option, according to May – membership in the customs union plus an extended version of the European Economic Area (EEA) – would be warmly welcomed by British industry and the financial community. It would, however, entail relatively free movement by EU nationals into the UK (and *vice versa*), significant contributions by the UK to the EU budget, and significant regulatory alignment with EU rules. Some form of all three of these ostensible drawbacks are likely to be present in any successful deal to maintain a free trading regime and close cooperation between the EU and UK, but they are anathema to the fanatically Eurosceptic European Research Group (or ERG) of Conservative MPs, and thus will not garner a majority in Parliament (without Labour support, which is presumed not to be forthcoming).

In mid-July the Prime Minister set out her own proposal, in a “White Paper” entitled *The Future Relationship between the United Kingdom and European Union*,² which is summarized below. But the contents of the White Paper were criticized, even before its publication, by a significant number of Conservative MPs, leading to multiple ministerial resignations and a growing sense that no Brexit deal would garner enough Tory support to be approved by Parliament, as required by the European Union

¹ <https://www.conservativehome.com/parliament/2018/08/mays-chequers-charm-offensive-continues-with-a-letter-to-tory-members-but-is-it-making-any-difference.html>.

² https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/725288/The_future_relationship_between_the_United_Kingdom_and_the_European_Union.pdf.

(Withdrawal) Act 2018³ (the “Withdrawal Act”). And the reaction to the White Paper in Brussels has been distinctly cool.

“No deal is better than a bad deal,” Theresa May has claimed repeatedly. This is almost certainly false, from an economic perspective, but it may be true for her from a political standpoint. Either “deal” purportedly “on offer” may cause her Government to fall. But it may also be the case that, even if the EU and UK negotiators are able to reach agreement on the framework for the future relationship between the EU and the UK after withdrawal, as required by the Withdrawal Act, Parliament will fail to approve that agreement as part of its “meaningful vote,” and as a result there will still be no deal.

This memorandum summarizes the current status of the negotiations between the UK and EU, and within each of the UK’s Conservative Party, the cabinet and Parliament, to explain why a “no deal” exit is unfortunately a real possibility. It then suggests some contingency planning that clients may want to implement as a result.

The risk of “no deal”

A range of public figures and bodies has warned of the risk of a “no deal” Brexit. Liam Fox (the International Trade Secretary) has put the odds of such an outcome at 60-40. Mark Carney (Governor of the Bank of England) has stated that “the possibility of a no deal is uncomfortably high” and is “highly undesirable.” Jeremy Hunt (the new Foreign Secretary, following the resignation of Boris Johnson) has said a ‘no deal’ Brexit “would be a mistake we would regret for generations.” And business organizations such as the CBI⁴ and many others have – in increasingly alarmed terms – warned of the substantial risks and economic damage of a “no deal” Brexit.

Adding fuel to the fire, late last week Philip Hammond, the Chancellor (i.e. the Government’s senior finance minister), reported to the House of Commons’ Treasury Select Committee that the Government’s January 2018 provisional analysis estimated that a “WTO/no deal scenario GDP would be 7.7% lower (range 5.0% - 10.3%) relative to a status quo baseline” under “the potential expected static state around 15 years out from the exit point.” His letter went on to estimate that “GDP impacts of this magnitude, were they to arise, would have large fiscal consequences,” including government “borrowing around £80 billion a year higher under a no deal/WTO scenario by 2033-34, in the absence of mitigating adjustments to spending and/or taxation.”⁵

³ http://www.legislation.gov.uk/ukpga/2018/16/pdfs/ukpga_20180016_en.pdf.

⁴ <http://www.cbi.org.uk/index.cfm/?api/render/file/?method=inline&fileID=AA65854F-A206-4B7D-A57764B16BE273F1>.

⁵ https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/735881/180823_CX_to_Chair_of_TSC_Nicky_Morgan.pdf.

On the same day as Hammond's warning, the UK government began publishing the first 24 of a series of 80 "technical notes" on the impact of no deal on a number of sectors of the economy.⁶ The EU has similarly published guidance on the severe consequences of there being no deal agreed.⁷ In the light of these developments, it is worth analyzing what "no deal" means, why the chances of this scenario have increased, and what steps might be taken to mitigate the associated risks.

What does "no deal" mean?

In broad brush terms, there are three variants.

No Withdrawal Agreement. One possibility would be a complete breakdown in negotiations – perhaps exacerbated by a political meltdown in the UK – that would result in the UK exiting from the EU on March 29, 2019 without a Withdrawal Agreement (and thus without a transition period). This could occur because of a failure to reach agreement on its terms, or because either the UK or the EU fails to ratify the agreement before March 29. This is considered unlikely, in part because many important aspects of the Withdrawal Agreement – including the transition period during which EU law and rules will continue to apply (until December 31, 2020), the UK's financial obligations to the EU, and the protection of rights of UK citizens in the EU and EU citizens in the UK – have already been agreed in principle.

But some important issues – such as the manner in which the border between the Republic of Ireland and Northern Ireland will remain open to the flow of people, goods and services – have not been resolved, and if the parties are ultimately not able to agree on the Withdrawal Agreement, or one side or the other refuses to ratify it, an economic and practical disaster would ensue. In this case, beginning on March 30, 2019 (among other things):

- tariffs would be imposed on trade between the UK and the EU, including significant tariffs on goods that are critical to the UK economy, such as agricultural products, automobiles and car parts;
- border inspections on either side of the English Channel (and along the 310-mile border between the Republic of Ireland and Northern Ireland) would be imposed, leading to what many have estimated to be multi-day waiting times and almost unimaginable border chaos;
- no specific protections would apply to UK citizens resident and working in the EU, and vice versa;

⁶ <https://www.gov.uk/government/publications/uk-governments-preparations-for-a-no-deal-scenario/uk-governments-preparations-for-a-no-deal-scenario>.

⁷ <https://ec.europa.eu/info/sites/info/files/communication-preparing-withdrawal-brexite-preparedness-web.pdf>;
<https://www.gov.uk/government/collections/how-to-prepare-if-the-uk-leaves-the-eu-with-no-deal>.

- unless separate stopgap agreements are reached in relation to these issues (which most people assume would happen, to avoid the chaos that would ensue in their absence), both airline travel and a large portion of freight transport between the UK and the EU would come to a halt;
- UK entities would cease to be eligible as EU entities for the purpose of receiving EU grants and participating in EU procurement procedures; and
- the UK will no longer have the benefit of over 750 treaties between the EU and third countries, including almost 300 trade agreements, over 200 agreements relating to regulatory cooperation, and scores of other agreements dealing with fisheries, transport (mainly airline services), customs procedures, nuclear energy, and agriculture. If not replaced on an emergency basis, the absence of several of these (e.g. in relation to air travel and the handling of nuclear fuel) would cause major disruption, at least in the short term.

The knock-on effects of this would be serious. To quote the *Financial Times*:

As well as raising a hard border on the island of Ireland – a political landmine – it would create enormous practical and legal uncertainties for businesses. ... Capital could flee the City of London, followed by a run on the pound. Food supplies would be at risk because of the uncertainty over certification and standards. The UK's ports and airports would be thrown into disarray. The list is endless, and no amount of wishful thinking can overcome this reality.

Most analysts still put the odds of this scenario at less than 50-50, but as both the UK and EU governments are now recommending that businesses plan for this disaster scenario, it cannot be ignored by the private sector any longer. And for the negotiators for both the UK and EU, this is the cliff edge that must be avoided on March 29.

Blind Brexit. To avoid this cliff edge, an increasing number of people are discussing a second “no deal” variant: a “blind Brexit.” A Withdrawal Agreement incorporating the transition deal would be put in place to avoid the March 29 cliff edge, but there would be no clarity on what the future trade relationship between the UK and EU will be after December 31, 2020, when the transition period is expected to end. This would postpone the day of reckoning, but would put both the UK Parliament and the UK's trade negotiators in an unenviable position. Parliament would need to approve the Withdrawal Agreement without knowing (except in vague, broad brush terms) what the UK's future trading relationship with the EU will be. Walking into a void may be better than stepping off a cliff, but it's hard to view this as a meaningful parliamentary vote on Brexit. And the negotiating leverage of the UK's trade negotiators, which is weak now, would be even weaker in such a scenario post-March 29.

It remains unclear whether the EU will be willing to accept a Withdrawal Agreement and framework for future relations that does not include a detailed “backstop arrangement” that avoids a hard border on the

island of Ireland. This was explicitly contemplated by a December 2017 “Joint Report” during the negotiations,⁸ and the European Parliament’s Brexit Steering Group has recently reiterated its insistence on the inclusion of that arrangement in any Withdrawal Agreement.⁹ That solution to the Irish border issue may be unacceptable to the DUP, however, and thus a “red line” that May and her government cannot afford to cross.

Parliament will in theory be free to reject a “blind Brexit,” but the alternatives will be frighteningly stark: the cliff edge (and economic disaster), or withdrawal of the Article 50 notice (assuming EU agreement) and thus no Brexit (and political disaster, unless that path has been legitimized by a second referendum or a new parliamentary election).

No Future Deal. A “blind Brexit” would avoid the March 29, 2019 cliff edge, but would increase the odds of there being no deal at the end of the transition period, currently expected to be December 31, 2020. Many in the UK government have articulated their desire for what some refer to as a “Canada plus” trade deal, which is shorthand for (to quote the Prime Minister again) a “bespoke model which meets the unique requirements of the United Kingdom.” Such an agreement is theoretically possible, but the EU-Canada deal took over seven years to negotiate, and covered a much narrower set of trade issues (for example, it did not cover services) than would need to be covered in a UK-EU agreement. The expected transition period is only 21 months long, and given the Conservative Party’s “red lines” and the EU’s fundamental negotiating principles, it is not clear that there is an unobstructed path to agreement on a range of issues. It is, moreover, not clear whether any trade deal that could be negotiated with the EU would satisfy a majority in Parliament, or would be better for Britain than not leaving the EU at all.

It is likely that, even if agreement upon a comprehensive trade deal proves elusive, in the period between now and December 31, 2020 a number of *ad hoc* agreements to avoid some of the more disastrous outcomes of a “no deal” Brexit could be hammered out. The problem is that there is no clarity on what those agreements would be, and thus which disasters would be avoided (and which would remain).

How did it come to this?

To understand the intractable complexity of the current situation, a little recent history is needed.

Chequers. A large part of the reason why there is so little progress to bringing clarity to the post-Brexit relationship between the UK and the EU is that the ruling Conservative Party is itself fundamentally split in its vision of the future. The British business community, traditionally a strong supporter of the Conservative Party, has become increasingly vocal in its advocacy of a “soft” Brexit, which preserves as

⁸ https://ec.europa.eu/commission/sites/beta-political/files/joint_report.pdf.

⁹ <http://www.europarl.europa.eu/news/en/press-room/20180727IPR08701/brexit-no-withdrawal-agreement-without-a-backstop-for-the-irish-border>.

much of the benefits of being in the customs union and indeed the single market as possible. A significant percentage of Tory MPs, reflecting these considerations, are fully supportive of a negotiated deal that retains these benefits and protects the UK economy in exchange for significant concessions in other areas. Another wing of the party, led by the ERG group of MPs noted above, is fundamentally opposed to anything that smacks of a “Brexit in name only,” including any commitments on free movement of people, any agreements to abide by EU regulations, any restrictions on the UK’s ability to negotiate trade deals with third countries, etc.

In an attempt to iron out the differences between these wings of her party, or at least to prevent them from breaking out in open internecine battle, the Prime Minister convened a meeting of her cabinet at her Chequers residence on July 6 to discuss and agree upon the general principles to be contained in the Government’s impending White Paper. After a long and reportedly heated day of talks, Theresa May hoped that she had broad agreement on the proposal that she was about to unveil, and released a statement outlining its general terms.¹⁰ Her hope was misplaced. In fact, within hours she was hit with a cascade of cabinet resignations, beginning with Brexit Secretary David Davis, followed by the Foreign Secretary Boris Johnson, the Parliamentary Under-Secretary for Exiting the EU Steve Baker, and a handful of other lower-level cabinet members. At the same time, Jacob Rees-Mogg, leader of the ERG group, savaged the impending proposals as being “worse than no Brexit.” These resignations and complaints created an ominous backdrop for May’s political standing.

White Paper. Notwithstanding these developments, on July 12, 2018, the UK Government published the White Paper, which sets out the Prime Minister’s vision of an economic and security partnership between the UK and the EU. The White Paper proposes, among other things:

- a free trade area for goods, to protect the integrated supply chains that span the UK and Continent, by adopting a “common rulebook for goods including agri-food, but covering only those rules necessary to provide for frictionless trade at the border;
- participation by the UK in those EU agencies that provide authorizations for goods in highly regulated sectors, such as the European Chemicals Agency, European Aviation Safety Agency and European Medicines Agency, so that the UK would have some ability to participate in the rule-making process in these areas; and
- the phased introduction of a “Facilitated Customs Arrangement” (or FCA) that would remove the need for customs checks and controls at the borders, which would allow the UK to control its own tariffs with third countries but allow goods to flow freely between the UK and EU.

¹⁰ https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/723460/CHEQUERS_STATEMENT_-_FINAL.PDF.

The White Paper confirmed the prior agreement in principle on the rights of EU nationals in the UK and UK nationals in the EU. It sidestepped issues relating to the ability of EU nationals to live and work in the UK after Brexit, however, other than to state that Brexit would “end free movement, giving the UK back control over how many people come to live in the UK,” and to note that details on the UK’s proposed domestic immigration rules would only be “set out in due course” after the release of the report of the Government’s Migration Advisory Committee in September.

The White Paper also did not propose a concrete replacement for the existing “passporting” regime for financial sector firms, while noting that it would no longer apply, and was similarly vague in relation to other services, causing consternation among many in the financial and other services sectors.

The White Paper’s key innovation – the Facilitated Customs Arrangement – is designed to address the Irish border issue, while at the same time allowing the UK to retain the benefits of being in a customs union while potentially retaining the right to strike separate free trade deals with other countries.

Customs Bill and Trade Bill. Weakened politically, May’s government then faced, less than a week later, the need to push two critical pieces of legislation through Parliament: a Customs Bill (officially the Taxation (Cross-border) Trade Bill) and a Trade Bill. These bills lay the regulatory framework for post-Brexit international trade by creating the power to collect tariffs and other customs charges and implementing international trade deals. Amendments to the Government’s drafts of these bills were submitted by both wings of the Conservative Party. Ultimately, both bills passed, but only just barely, and with amendments proposed by the hard-Brexit wing of the party that (among other things) would undermine the UK’s ability to implement the Facilitated Customs Arrangement proposed in the White Paper. Theresa May narrowly avoided a humiliating Commons defeat, but at the cost of signaling to EU negotiators that the UK Government was still deeply divided and that May might not have the votes to deliver on her proposals.

EU Response. The EU’s lead Brexit negotiator, Michel Barnier, responded to the White Paper and the surrounding Westminster political noise with restraint, but clear skepticism. He stated that “there are some elements [of the White Paper] which do seem to contradict the guidelines of the EU council,¹¹ the heads of government and state, namely the indivisibility of the four freedoms and the integrity of the single market,” and expressed his opinion that “[t]here is not a lot of justification for the EU running the risk of weakening the single market.” He also noted that the White Paper “is the result of a very intense debate in the United Kingdom” and “everyone can see that this debate is not over.”

Among other things, Barnier cast severe doubt on the practicality of the Facilitated Customs Arrangement, while a number of EU diplomats reportedly said privately that the arrangement would never be accepted.

¹¹ <http://www.consilium.europa.eu/media/33458/23-euco-art50-guidelines.pdf>.

As the EU has stated on numerous occasions that finding a solution to the Irish border issue is a *sine qua non* in any Brexit agreement, the possibility of this issue leading to an impasse is of great concern.

There are other thorny issues to be resolved as well. A number of EU countries will be extremely focused on the ability of their nationals to live and work in the UK. Spain is very focused on the status of Gibraltar post-Brexit. And all EU countries with internal Eurosceptic political pressures will be loath to give the UK a deal that might seem attractive and thus encourage secessionist tendencies. These competing priorities are of critical importance when one considers that a super-majority affirmative vote of 20 of the 27 votes to be cast is needed to approve any withdrawal agreement.

What happens between now and March 29?

September. With key issues yet to be resolved (including the fraught issue of the Northern Ireland border), and Brexit Secretary Dominic Raab and Michael Barnier recently pledging to “negotiate continuously from now on,” September looks to be an important month for UK-EU negotiations. Politically it may also be a challenging month, as Parliament returns from recess on September 4th, and with both the Labour Party conference (September 23rd-26th) and Conservative Party conference (September 30th- October 3rd) approaching, it is foreseeable that political posturing will exert strong influences both on the Tories and on Labour.

The Labour Party has, until now, been only a muted participant in the Brexit debate, in part due to the limited power of any party in opposition in the UK parliamentary system, but also due to the (at best) lukewarm attitude of the Labour leader, Jeremy Corbyn, towards the EU. The party has said it “accepts the referendum result” but “will scrap the Conservatives’ Brexit White Paper and replace it with negotiating priorities that have a strong emphasis on retaining the benefits of the Single Market and Customs Union – which are essential for maintaining industries, jobs and businesses in Britain.”

Oddly, this aligns Jeremy Corbyn – an avowed socialist – with the CBI and other business organizations. But there is a growing groundswell within Labour, especially among the younger Momentum members within the party who swept Corbyn to power, to take the further step of calling for a second referendum (now being referred to as a “People’s Vote”). Labour’s leadership has resisted this, hoping instead for May’s government to fall as a result of right-wing rebellion at the White Paper’s proposals (as they may move even further towards the position promoted by Labour, but deeply objectionable to the ERG), and to have a chance at power in a new election. Last week, though, Labour’s Brexit spokesman, Sir Keir Starmer, is reported to have suggested a “second referendum should be on the table” if Parliament votes down the Brexit deal. The tactical benefits (and drawbacks) of calling for a second referendum are likely to be topics of heated discussion at the Labour Conference, and could well be the subject of a vote at the Conference.

The other key thing to look for is the release of the report of the Migration Advisory Committee. This report, now arguably over a year overdue, has been delayed repeatedly due largely to Conservative Party infighting.

A number of business, farm and other groups in the UK have called for the government to embrace a fairly open immigration policy towards the EU. This would be very helpful in facilitating agreement on the Withdrawal Agreement. For the ERG, and many who voted in favor of leaving the EU, restricting the inflow of immigrants from the EU was a key reason for Brexit, and therefore many Tory backbenchers are likely to resist an open policy.

October-November. The key date in October is that of the European Council meeting on the 18th. That was to have been the date on which a final draft Withdrawal Agreement was to be presented for consideration. If that date passes without agreement, which seems likely, there was then an ostensible October 31 “deadline” for finalizing a deal. Managing expectations, the Cabinet Office has now admitted that too may no longer be a realistic deadline, and the EU’s Michael Barnier stated last week that it would not be a problem if the talks slip into November, provided that they be wrapped up “not much later than that.”

If by the end of October the negotiators are not, however, perceived to be converging on an agreement that would appear likely to survive in Parliament, increasing expressions of alarm from the business community, and perhaps increasingly vocal calls for a fundamental rethinking of policy alternatives, seem likely.

December. December 13-14, 2018 are the dates of the last European Council meeting in 2018, and thus the last practicable date for a Withdrawal Agreement and an framework for future relations (however vague) to be agreed between the EU and UK (absent an extraordinary meeting of the Council). If the October deadlines are missed, as is now expected, and there is still the will on both sides to try to reach agreement, there will be tremendous pressure to do so by these dates in mid-December.

What happens next? If agreement is reached by December, the Withdrawal Agreement and framework then need to be submitted for approval by the relevant EU authorities and by Parliament.

On the EU side, the agreement will require the consent of the European Parliament (voting by simple majority) and approval by a qualified majority (20 of 27) of the European Council (representing the EU member states; the vote must represent 72% of the 27 remaining member states and 65% of the population). Under the Withdrawal Act, the Withdrawal Agreement and framework for the future relationship must be presented to both Houses of Parliament (Commons and Lords) and be approved by a resolution of each House, and an Act of Parliament must then be passed which provides for the domestic implementation of the Withdrawal Agreement. If possible, the House of Commons is supposed to debate and vote on the Withdrawal Agreement before the European Parliament is asked to consent to the agreement. The Withdrawal Bill sets a deadline of January 21, 2019 for the Brexit vote.

If the House of Commons does not pass the resolution approving the Withdrawal Agreement, the Government must within 21 days make a statement in writing setting out what the Government proposes to do (including whether it still proposes to ratify the treaty represented by the agreement). After such

statement is delivered, Parliament has another 21 sitting days to decide what it wants to do in response. This is one scenario in which either a new election might be called, or a second referendum demanded, to break through what would otherwise be a constitutional impasse.

If the Government concludes that it will not be able to reach agreement on the Withdrawal Agreement and framework on terms that it finds acceptable, or if agreement is not in fact reached by January 21, the Withdrawal Act requires the Government to make a statement to Parliament setting out how the Government proposes to proceed, and to make arrangements for a motion “in neutral terms” to be presented to the Commons in respect of its recommended course of action. This is another scenario in which a new election, or a second referendum, might arise.

A Second Vote?

While recent polling data shows a growing percentage of the British electorate would support a second referendum, and the percentage of support may reach an absolute majority if the alternative is a “no deal” exit, at present neither the Conservative Party nor the Labour Party supports a second vote. Brexiteers are fearful – rightfully so, based on recent polling data – that a second referendum might go the other way, and so they react with unrestrained outrage at any suggestion of a second vote, claiming that this would somehow be an affront to democracy (even though the first referendum was explicitly non-binding and a second referendum would presumably be as “democratic” as the first). For a different reason Labour is also not pushing a second vote. Corbyn and his allies would rather have a new election, in hopes that they might win, and are fearful of losing some working class Leave votes, although recent data suggests that it has more to fear in the other direction. (The Liberal Democratic Party has called for a second referendum since December 2017, but the Lib Dems are too weak to swing this debate.)

Politics aside, there are at least three significant challenges to holding a second referendum. The first is that the level of rancor – and risk of political violence – that might surround the vote would be high.

The second challenge is the formulation of the question. If there is no deal the choices are clear: Leave with no deal, or Remain. If there is a Withdrawal Agreement and framework, but they have been rejected by Parliament, then there are three possible answers: accept the agreement; Leave with no deal; or Remain. But the chance that no option would receive a majority means that a “first past the post” format to such a vote would run a high chance of an ambiguous, result. A range of suggestions, some of which are clever,¹² have been made to address this conundrum, but there is no way to deny its complexity.

¹² See, e.g., V. Bogdanor, *Brexit broke parliament. Now, only the people can fix it*, at https://www.theguardian.com/commentisfree/2018/jul/23/brexit-broke-parliament-people-fix-election-dilemma?CMP=aff_1432&awc=5795_1534783172_f8ad215b049ab7433afc041803d066ed

The third challenge is that the procedure for calling and holding a referendum in the UK, which is set out in the Political Parties, Elections and Referendums Act 2000,¹³ requires an Act of Parliament, an assessment by the Electoral Commission of the intelligibility of the proposed referendum question(s), and a ten-week regulated campaign period. Under ordinary circumstances, then, Parliament would need to pass legislation calling for the referendum in November in order to have the vote before March 29. As the crisis points noted above are all likely to be in December or January, and it is highly unlikely that the current Government would acquiesce in calling a second referendum other than in response to a crisis (where a second referendum would be the least worst outcome), there will not be sufficient time before March 29. This means that either the Electoral Commission would need to pass on the question presented in far less than 10 weeks, or the Act providing for the second referendum would need to shorten the statutory timetable, or the EU would need to extend the March 29 deadline to accommodate the referendum. Each of these solutions is possible, but far from assured. As a result, the reality may be that there simply isn't sufficient time.

What is to be done?

There was hope, at the outset of the Brexit negotiation process, that as time went on the nature of the relationship between the UK and the EU, and its impact on businesses and people, would become clearer. In several important respects, not only has this not happened, but the range of possible outcomes has actually widened.

Both the EU and the UK are now advising businesses that, given the tremendous uncertainty, there is an urgent need for all firms to adopt contingency plans for all outcomes. Particularly in certain sectors, the potential adverse impact of a “no deal” exit will be sufficiently severe to disrupt supply lines, exacerbate exchange rate exposure risks, temporarily dry up sources of funding, and in some cases cause a (probably only temporary, but still potentially fatal) cessation of business.

Businesses with significant UK operations, suppliers, customers or clientele, should assess the potential negative impact on their operations in a no deal scenario, and identify any steps that might be taken to mitigate or otherwise respond to the perceived risks. Several sector specific business associations have now published guidance designed to assist members to plan for a “no deal” scenario. The so-called technical papers being published by the UK Government, although criticized by some for their vagueness, also contain some useful sector-specific information. To summarize some of the more useful guidance from these various sources:

Forex risk. The pound has declined against the dollar from \$1.48 on the day before the referendum to about \$1.28 at today's rate, but some analysts have projected a further slide to as low as parity in a no deal scenario. While sterling's decline may be beneficial for those purchasing pound-denominated goods and

¹³ <https://www.legislation.gov.uk/ukpga/2000/41/contents>.

services, or whose functional currency is sterling but are selling dollar-denominated goods and services, British operations that are reliant on euro or dollar-denominated supplies will want to consider whether they are adequately hedged.

Supply chain disruption: A recent study by Imperial College London concluded that adding only two minutes per vehicle at the borders, for customs and security checks, could result in backups on the highways near the borders of 29 miles during peak times, causing serious disruption to supply chain management and rendering impossible just-in-time inventory management. Special problems may be encountered in relation to regulated products such as pharmaceuticals, leading the British Medical Association to call for a second referendum.¹⁴ Similar fears have been raised in respect of food supply chains. To the extent not already underway, businesses with supply chains that span the UK-EU border should consider assessing as soon as possible their exposure to these risks and determine whether any identified risks can be mitigated through arrangements with alternative suppliers, the stockpiling of inventory, or other measures.

Trading Mechanics. In a no deal scenario, firms that import goods from the EU to the UK will need to follow customs procedures in the same way that they do in importing good from other countries. Similarly, firms that export goods from the UK to countries the EU will need to follow customs procedures in each such country applicable to non-EU trading partners. Companies that already have well-developed trading operations may be able timely to adapt to the new environment, particularly if contingency plans are initiated now. Those that have smaller back office capabilities may now want to assess whether they need to bolster their in-house capacities (in terms of personnel, software, etc.) or are instead better served by putting in place arrangements with a customs broker, freight forwarder and/or logistics provider to support their trade-related activities in this scenario.

EU regulatory authorizations: Most large-scale financial services firms have already confirmed that their European footprint is sufficient to continue operations under non-UK regulatory authorizations and/or licenses that will continue to enjoy “passport” rights throughout the EU post-Brexit, or have taken steps to identify an existing, or organize a new, affiliate in another EU country that can apply for such authorizations. This will often entail the relocation of sufficient staff to meet the minimum oversight and staffing requirements in that other jurisdiction. Many firms that are not primarily engaged in financial services, however, such as retail operations that provide consumer credit, or advisory services that include a regulated financial element, may have to date been less focused on their need for a post-Brexit solution, in light of the anticipated transition period to December 31, 2020. As the cushion afforded by the transition period is not assured (if there is no deal, there is no transition period), firms with the need for an EU

¹⁴ <https://www.bma.org.uk/collective-voice/influence/europe/brexit/overview>. See also <file:///C:/Users/00182/Downloads/BMA-briefing-regulation-of-medicines-medical-devices-and-substances-of-human-origin-after-Brexit.pdf> (outlining range of UK-EU agreements necessary to avoid disruption to the UK medical profession and patients).

passport-able license should consider developing contingency plans for the scenario where the anticipated transition period is unavailable.

Because the termination of the right of EU/EEA financial sector firms that currently operate in the UK under the passport regime to offer services on March 30, 2019 would cause significant market disruption, the UK has announced that it will introduce a Temporary Permissions Regime that will allow EU firms (and also those from Iceland, Liechtenstein and Norway, which are members of the EEA but not the EU) to continue operating in the UK for up to three years after exit. The Government has also committed to introduce legislation that will provide that contractual obligations (such as insurance contracts) between EU/EEA firms and UK-based customers that are not covered by the Temporary Permissions Regime will remain legal and enforceable. If other countries in the EU, or the EU itself, were to put in place similar temporary measures for the benefit of UK firms, this would significantly reduce the short-term regulatory chaos that would otherwise ensue in a no deal scenario, but there is at present no assurance this will be implemented or that, if approved in principle, such a regime can actually operate as if a deal had been reached, due to the complex legal and regulatory issues involved.

EU workers: Many sectors in the UK economy, including agriculture, healthcare and retail operations, are reliant on EU workers, both skilled and unskilled. Many businesses in these sectors are predicting significant constraints due to worker shortages if immigration from the EU is tightened considerably in a no deal scenario. While this is not likely to have a significant effect on multinational firms outside these sectors, businesses should consider whether suppliers or customers may be materially affected.

Communications with stakeholders: Public companies in particular need to be mindful of disclosure obligations and, in particular, their risk factor disclosures. If past history is any guide, securities regulators will increase their focus on these disclosures as the likelihood of a no deal increases. These companies should be mindful of all of the potential implications of potential Brexit outcomes, including collateral consequences, for example, capital and liquidity needs that could be triggered by the implementation of contingency plans.

Given the range of possible outcomes, it is equally important that businesses not over-react. Many observers still believe that the risk of a cliff edge exit remains low, so while contingency planning is warranted, firms should consider postponing implementation of costly or irreversible actions until the earlier to occur of the date on which it becomes clear that they will be needed, and the latest date on which they can safely be implemented in time to mitigate the risk they are intended to address.

With the level of uncertainty surrounding the Brexit process increasing, it is unfortunately not possible at this juncture to provide any clear guidance on, let alone predict, likely outcomes. Some version of a “no deal” exit is possible. A second vote, leading to no Brexit is possible. And a negotiated Brexit, which is not 100% satisfactory to anyone but avoids serious harm and allows an orderly transition and on rational future relationship, is also possible. It is also likely that at March 29, 2019 the full details of that future relationship

will not be known. That in turn means that, even in the best of circumstances, even on March 29, 2019, there is still likely to be uncertainty as to the ultimate nature of the relationship between the UK and the EU. As a result, businesses may need to adapt their responses to changing circumstances over what may be a protracted period of negotiation lasting well into 2020.

We will continue to monitor these developments. If you have questions, please feel free to contact either of the undersigned.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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