

BREXIT

Board Briefing

AUGUST 2016



The world is awash with uncertainty about Brexit. We imagine that you, like most, are sorting through it all. Pillsbury is here to help. Our dedicated Brexit Team is monitoring developments and weighing the legal risks and opportunities that will likely arise from the impending UK withdrawal. For now, rather than wax on about things that are not yet knowable, we have created a high level briefing. This is a basic primer for executives and directors, outlining in plain English some of the critical short- and long-term legal issues that entities conducting business across borders will likely need to consider as a result of the Brexit vote.

For a deeper dive on any of the legal issues noted in the briefing, we encourage you to contact any member of the Brexit Team or visit our online **Brexit Resources Center**. If our Board Briefing does not address a legal area that your organization is particularly concerned about, please let us know. Our research team will look into it and share their findings with you.

Sincerely,



Tim Wright

London Office Managing Partner and Brexit Team Leader
tim.wright@pillsburylaw.com

Surveying the Post-Vote Landscape

Businesses face a sustained period of uncertainty and potential disruption in the wake of the UK's Brexit referendum vote. The consequent volatility in financial markets, a weakened pound, historically low interest rates and fresh monetary stimulus measures by the Bank of England set an ominous economic and political stage against which future investment and operating decisions must be made.

But amid the turmoil, Brexit also has given rise to opportunities for businesses and for investors. For example, The Times of London recently reported that after the sharp post-vote sell-off, directors across the FTSE 350 bought up large amounts of stock in their own companies. These executives reportedly spent some £18.5 million of their own cash across a range of blue chip companies including Marks and Spencers, Royal Mail and EasyJet.

In the uncertain aftermath of the Brexit vote, businesses must understand, assess and strategize for the particular issues their businesses face. They must also take advantage of this chance to strengthen their business position and safeguard their long-term future.

Assessing Potential Impacts

As has become painfully clear, the UK government had no plan for Brexit and is only now starting to develop its exit strategy. Businesses cannot afford such complacency. Although the actual mechanics by which Brexit will be achieved—and the precise model which Brexit will take—are still to be determined, businesses with European interests and activities should consider putting in place a broadly constituted Brexit project team.

All areas of the business should be represented including finance and treasury, indirect and direct tax, legal, commercial, corporate and company secretarial, regulatory compliance, human resources, sales and marketing, technology and PR/communications, as well as representatives from the main business units. The team should start by focusing on their enterprise's operating model, business interests and activities within the UK and the EU. They should model the various scenarios for Brexit, assess the potential risks and opportunities and apply those takeaways as a favoured Brexit model emerges. The project team should be suitably empowered with C-level buy-in and, as appropriate, participation of key stakeholders.

Planning for Brexit

Brexit has the potential to impact many aspects of international business, including the possibility of supply chain disruption as the legal and regulatory consequences of withdrawal begin to materialise. One of the first tasks of the Brexit project team as it gets up to speed should be to pull together a project plan. This plan should cover each function within the business that could hypothetically be affected by Brexit, considering European subsidiaries and branches, EU regulatory licenses and authorisations, EU-based counterparties, international trade flows, international supply chain and logistics arrangements, EU-wide distribution and franchise arrangements, and other market channels.

Communication is Critical

A robust communications strategy—covering internal and external announcements as well as other important messaging channels—should be included in the broader Brexit plan. Legal requirements to inform and consult with employee representatives and workers councils at appropriate times also warrant serious consideration.

Preparing a Legal Analysis

In-house counsel and trusted outside legal advisers have key roles to play in Brexit planning as well. Whilst the UK remains a member of the EU for the time being—and will therefore continue to be governed by EU law until exit negotiations are finalised—some of the key areas to be considered include:

Antitrust & Competition

Post-Brexit, EU competition rules will continue to apply to the agreements and conduct of UK companies with operations inside the EU. Longer term, however, there is likely to be a significant change to the UK competition law regime. The removal of the “one-stop shop” for mergers within the UK and EU notification thresholds and the falling away of the Commission block exemptions are widely anticipated.

Business Immigration

Businesses that currently employ large numbers of non-UK EU nationals working in the UK or significant populations of UK nationals based in other EU member states may be particularly affected by Brexit. These companies will need to pay particularly close attention to which model is adopted by the UK and whether it results in an end to the freedom-of-movement rules.

Capital Markets

Capital markets in the UK and the rest of the EU are deeply intertwined and are primarily governed by EU legislation such as the Prospectus Directive, the Transparency Directive and the Market Abuse Regulation. The impact of Brexit on securities offerings will largely depend on the final terms of withdrawal. Any major discrepancy between the UK and EU's respective approaches to capital markets will have a significant impact on the investment climate throughout Europe. Should the regimes diverge, it is possible that all but the largest issuers will forego the extra cost and effort of preparing multiple prospectuses and focus instead on one market, effectively shutting UK investors out of EU investment opportunities and significantly reducing The London Stock Exchange's market share. The UK's loss of mutual recognition rights in the EU may have a similarly damaging effect on debt securities by making public offerings within the EU significantly more difficult. The UK will most likely endeavour to maintain close consistency with EU requirements in order to preserve its status as a major financial centre, but doing so may be easier said than done.

Commercial Contracts

Any large organization will have a myriad of commercial contracts with a wide range of counterparties, many of which will be located within the EU. Businesses should make identifying such contracts—which have both an international dimension and are critical to a company's operating/regulatory standing—a top priority. These contracts can then be grouped into categories such as joint ventures; IT and business process outsourcing; cloud computing; software licenses; software development; franchise and distribution; supply of goods, commercial agency; real estate and construction. Where there are large volumes of contracts to be reviewed, consider engaging an outside law firm or other legal provider to do this, establishing in advance clear parameters for review of potentially impacted provisions. These would include material adverse change clauses, currency exchange, price adjustment, compliance with laws and territorial definitions. Key counterparties whose businesses may be adversely impacted by Brexit should also be identified.

Once this classification is completed, each contract can be reviewed by appropriate parties. Some will need to be renegotiated, others may no longer be viable at all post-Brexit and should therefore be considered for termination. Businesses may wish to develop a playbook for renegotiations, as well as template clauses for inclusion in commercial contracts over the next few years, where the potential impact of Brexit is still not known and the option to review the arrangements at some point on the future needs to be built-in.

Consumer Contracts

Businesses which sell directly to EU consumers will likely be significantly impacted, especially if the adopted Brexit model sees the UK leave the single market. Much of the UK's consumer protection laws come from the EU (such as flight delay compensation and mobile roaming charges) as do laws and regulations relating to advertising and marketing, product liability and labelling (e.g., the recently implemented plain packaging rules for tobacco products). Further, if the UK loses its passporting rights into EU member states, it may no longer be legal to perform particular insurance and other affected financial services contracts.

Crypto Currencies

Crypto currencies have become somewhat of an unlikely haven for investors, with bitcoin and other digital currencies surging in value following the Brexit vote (though this may have been dampened by the recent \$61 million hack of the Bitcoin exchange Bitfinex). Businesses using digital currencies need to become familiar with the unique regulatory issues associated with this technology. They must also keep abreast of potential regulatory changes like the loss of the so-called "financial passport," which will impact companies in the digital currency space as well as the wider financial services sector. In addition, newly introduced legislation—such as the anti-terrorism-financing directive proposed by the European Commission that would make virtual currency users' identities and wallet addresses accessible to government financial intelligence units—could also lead to rapid and substantive changes in the regulatory framework surrounding digital currencies.

Cybersecurity

The Cybersecurity Directive will come into effect by 10 May 2018 and sets out security obligations for operators of essential services such as transport, health and finance, as well as for digital service providers like online marketplaces, search engines and cloud services. It is likely that the UK government will enact similar cybersecurity laws in the UK to avoid trade restrictions in the future.

Data Privacy

Whilst Brexit does cast a shadow over the current methods used to support the lawful processing and transfer of EU personal data, businesses will already be grappling with the need to comply with the new EU General Data Protection Regulation (GDPR) from 25 May 2018. Recent discussions with EU privacy commissioners suggest that updated UK-specific data protection legislation will closely mirror EU data laws. Businesses will therefore need to conform to new GDPR

Brexit

requirements but also any exception or variation that may be introduced specifically for the UK, since the UK will become a “third country” upon its withdrawal from the EU. This means that EU data flows to the UK will cease to be “automatically safe.” Individual businesses should take steps now to review and enact changes to internal processes and policies to meet the new privacy-by-design requirements, as well as develop revised contractual provisions which reflect the GDPR regime.

Disclosures and Reporting Requirements

Brexit-related risk factors may need to be noted in corporate reports and prospectuses. The UK Financial Reporting Council recently issued guidance in this respect relating to annual and half-yearly financial reports. In accordance with that advice, boards of directors need to determine whether to make any disclosures in their financial statements, as well as management and strategic reports. Such disclosures need to meet the needs of investors and comply with applicable regulatory requirements and, according to the Financial Reporting Council, should potentially cover the business model; principal risks and uncertainties; market volatility; going concern basis of accounting; and true and fair view. In their half-yearly reports, directors should also consider important events that occurred during the first six months of the financial year. Outside of the UK, there will be similar concerns for international businesses (for example, Securities and Exchange Commission disclosure obligations in the United States). The greater the exposure to the UK and EU markets, the more robust the disclosure required.

Dispute Resolution

Brexit will have a direct—but not yet clear—impact in the disputes arena. Current UK law is governed by a framework of EU legislation (such as the Rome Conventions) which set out the rules that courts in EU member states must apply when determining the governing law of a contract and of tort (e.g. negligence) claims. This includes their jurisdiction to hear disputes, the procedures for serving legal proceedings and the mechanics for enforcing judgments in other member states.

Employment

The UK’s employment law is an intricate mix of national law and EU law. Whilst the Brexit vote does not signal an immediate end to statutory employment rights for UK employees and workers, it will instead serve as a starting point for a specific review of how statutory employment protections should be applied in the UK going forward. Certain employment rights which are currently mandated by the EU are perceived to be unnecessarily bureaucratic by the UK government, and these will likely receive heavy scrutiny. Repeals of the Agency Workers Regulations 2010 and certain aspects of the Working Time Regulations 1998—both of

which were transposed into UK legislation as a direct result of EU directives—are widely anticipated. A cap on potential compensation for unlawful discrimination could be added to the Equality Act 2010, and TUPE may be amended to enable employers to make changes to terms and conditions of employment post-transfer. Changes to the obligations to inform and consult employees may also be investigated, as these are often seen as unnecessary red tape.

Environment & Property

Brexit will likely make a dramatic impact in this area, since the UK’s environmental laws are largely derived from EU law (with the exception of the Climate Change Act 2008). Though some areas of law are governed by international conventions and treaties—to which the UK is already signatory—commentators have described the task of unpicking UK environmental legislation to separate out and rewrite legislation implemented by the EU as potentially “enormous.” In the future, there may be changes to property rules deriving from EU legislation, such as energy performance certificates (EPCs), minimum energy efficiency standards (MEES) and green leases. Indeed, more than a little change appears to be on the horizon.

Financial Services

London has long been viewed as a gateway for US and Asian companies into Europe, and a key reason for this has been the success of the passporting regime, which enables UK-based financial institutions to carry on financial services activities covered by an EU single market directive (such as MiFID and Solvency II) in another European Economic Area (EEA) member country without explicit authorization from each local regulator. To be sure, cross-border unsecured and secured lending, guarantees, bond issuance and sale, medium-term notes, commercial paper, derivatives and structured finance all rely on passporting to some degree. If the UK loses its passporting rights, London’s position as a critical financial centre and a hub for companies seeking to do business across European markets will be put in jeopardy.

Intellectual Property

Should the UK remain a member of the EEA post-Brexit, the laws governing intellectual property rights in the UK would remain more or less the same. Full departure, however, would have substantial ramifications for IP rights holders, across a number of disciplines. Barring the creation of a mechanism to effectively transition existing intellectual property into UK law, EU trade marks and designs would cease to be protected in the UK, and the UK courts that govern them would no longer have jurisdiction to hear EU disputes. The EU Trade Mark Directive and Unitary Patent system would most likely come off the books. Existing IP contracts would require comprehensive review, with territorial scope provisions of licenses and

assignments requiring close analysis to ensure appropriate UK coverage. And more broadly, because the UK would no longer be bound by European copyright and patent decisions, withdrawal could precipitate a macro-level divergence between EU and UK application of IP law. While the specific effects of Brexit on intellectual property rights in the UK has yet to be determined, there are numerous potential outcomes for which rights holders should prepare. Companies would be wise to consider all possible outcomes and game plan accordingly.

International Trade

Upon leaving the EU, the UK will need to negotiate a host of new international treaties governing a long list of trade partners. On a case-by-case basis, the government will have to develop and set new trade rules regulating tariff rates, market access, dispute resolution methods and more. Further, despite continued status as a member of the World Trade Organization, the UK must pursue bilateral arrangements to further serve the needs of its export sectors and domestic industry – something the UK has not needed to do for a generation. Companies will need to understand the impact the loss of EU trade and EU trade deals with nations outside of the block will have on their business and work to make sure that new deals being pursued by the UK government serve their interests. They must know the new ways in which trade disputes will be handled and be prepared to rely more on their own capabilities and less on government. Sophisticated organizations will begin this process early in order to ensure their seat at the negotiating table.

Mergers & Acquisitions

Post-Brexit turmoil has undoubtedly taken a toll on the UK M&A market, with activity values dropping 51 percent in Q2 and expected to fall even further in the second half of 2016. M&A valuations and transactions are being reconsidered, whilst companies eager to establish a European presence may contemplate other jurisdictions in which to base their hubs. This uncertainty does not mean that M&A activity will grind to a halt. The structure and execution of UK private M&A transactions, for example, should not be materially impacted by Brexit. And the current investment climate may actually present significant opportunities for non-UK businesses shopping for a relative bargain. Longer term, deal volume will largely be dictated by merger regulations, trade agreements, and London's future role in the global economy. Decisions affecting the UK's future relationship with Europe are out of the hands of those at the forefront of the M&A market for the time being. Businesses should not panic, however. The UK government will not wish to make the UK unattractive for businesses and is therefore expected to work hard to maintain the UK's strong position as an investible jurisdiction.

Public Sector Procurement

In the immediate wake of the Brexit vote, the English law regime applicable to public procurement remains unchanged. The long-term outlook, however, depends heavily on the way in which the UK exits the EU. While the Procurement Directive ensures British firms competing for public procurement contracts in EU member states will continue to have access to the public procurement market in the near-term, the utilities and defence sectors already have rules in place that allow those markets to be closed to bidders from non-EU countries.

Project Finance & Development

Brexit is likely to have a significant impact on UK-based infrastructure and other projects, as well as the involvement of UK companies in projects elsewhere on the continent (and possibly in even broader jurisdictions). The pending exit from the single market is likely to delay or, in some cases, halt international investment in UK projects. As a result, the cost of debt financing may grow higher. Many UK projects also receive funding from the European Investment Bank (EIB) — approximately €7.8 billion in 2015. It remains to be seen how Brexit will affect projects expecting funding or guarantee facilities from the EIB and, perhaps more importantly, how the UK will bridge the funding gap.

Restructuring & Insolvency

EU insolvency law is somewhat harmonised, with the Insolvency Regulation providing for procedural co-ordination and automatic recognition of insolvency proceedings across different EU jurisdictions. Post-Brexit, the UK's implementing law will cease to apply, meaning that debtors in UK insolvency proceedings may be exposed to additional insolvency proceedings in the EU, rather than a single pan-EU proceeding.

Tax & Customs Duties

Membership in the EU has had a fundamental effect on the UK tax code. It absolved the UK from paying customs duties within the EU; allowed the country to share the expense of common tariffs with its fellow member states; and granted it a not-insignificant distribution of the VAT funds collected across Europe. In the wake of the Brexit vote, however, that could all change. The possible scrubbing of some rules—like the Parent-Subsidiary Directive, the Royalty Directive and the Merger Directive — would have a significant financial impact on European companies operating in the UK. New rules will need to be developed to address VAT. And exports between the UK and the EU will be subject to as yet undetermined procedures and, potentially, customs duties. Post-Brexit, the tax relationship between the UK and EU member states is uncertain at best. Businesses must review their international tax strategies and make sure that they are structured in a way that enables the flexibility to adapt to a future still in flux.

Brexit Resource Center

For more in-depth views on the Brexit-related legal issues that could affect your business, we invite you to review our online **Brexit Resource Center**, where we will continue to provide new insights in the weeks and months to come. You may also email brexit.support@pillsburylaw.com with general inquiries or reach out directly to one of the Brexit team members identified here.



Tim Wright
London Office Managing Partner and Brexit Team Leader, Global Sourcing, London
 +44.20.7847.9505
tim.wright@pillsburylaw.com



Steven P. Farmer
Counsel, Global Sourcing
 London
 +44.20.7847.9526
steven.farmer@pillsburylaw.com



Rafi Azim-Khan
Partner, Intellectual Property, Data Privacy
 London/Silicon Valley
 +44.20.7847.9519
rafi@pillsburylaw.com



Caron Gosling
Counsel, Employment
 London
 +44.20.7847.9529
caron.gosling@pillsburylaw.com



Sandra Bates
Partner, Corporate & Securities
 London
 +44.20.7847.9540
Sandra.bates@pillsburylaw.com



Matthew Oresman
Counsel, Public Policy
 London/Washington, DC
 +44.20.7847.9516
matthew.oresman@pillsburylaw.com



Stephan E. Becker
Partner, International Trade
 Washington, DC
 +1.202.663.8277
stephan.becker@pillsburylaw.com



Samuel J. Pearse
Partner, Corporate & Securities
 London
 +44.20.7847.9597
samuel.pearse@pillsburylaw.com



Tina Blazquez-Lopez
Counsel, Finance
 London
 +44.20.7847.9577
tina.blazquezlopez@pillsburylaw.com



Mike Pierides
Partner, Global Sourcing
 London/Abu Dhabi
 +44.20.7847.9559
mike.pierides@pillsburylaw.com



James Campbell
Partner, Corporate & Securities
 London/ Abu Dhabi
 +44.20.7847.9504
james.campbell@pillsburylaw.com



Graham Tyler
Partner, Finance
 London
 +44.20.7847.9562
graham.tyler@pillsburylaw.com



Anne Fairpo
Advisor, Tax
 London
 +44.20.7847.9611
anne.fairpo@pillsburylaw.com

ATTORNEY ADVERTISING. Results depend on a number of factors unique to each matter. Prior results do not guarantee a similar outcome.

Pillsbury Winthrop Shaw Pittman LLP | 1540 Broadway | New York, NY 10036 | 877.323.4171

pillsburylaw.com | © 2016 Pillsbury Winthrop Shaw Pittman LLP. All rights reserved.

Abu Dhabi • Austin • Beijing • Hong Kong • Houston • London • Los Angeles
 Nashville • New York • Northern Virginia • Palm Beach • Sacramento • San Diego
 San Diego North County • San Francisco • Shanghai • Silicon Valley • Tokyo
 Washington, DC