BREXIT BRIEFING

Eight months to Brexit: is your business prepared?

As the clock ticks down to 29 March 2019, the UK and the EU are stepping up their preparations for the possibility of a "no-deal" outcome. Businesses must do likewise.

In March 2018, political agreement was reached on the broad terms of a transition period up to the end of December 2020. During this period, the UK would continue to apply most EU law without any amendments and accept the authority of the Court of Justice of the European Union, the European Commission (the Commission) and other EU regulators.

However, the need for the European Council and both the EU and UK Parliaments to approve the final form of the withdrawal agreement and the political declaration on the framework for the future UK-EU relationship means that the possibility of a no-deal Brexit in which the UK leaves the EU abruptly at the end of March 2019, with no transition period, remains a real possibility. It will be some time before we know which way it will go.

Brexit assurance process

There are three principal phases to a Brexit assurance process:

- Conducting an audit of the no-deal implications to pinpoint risks and opportunities.
- Evaluating and prioritising the audit conclusions to create a Brexit readiness plan. A plan should identify key deliverables and their lead times, include a timeline and allocate resources to meet Brexit readiness deadlines.
- Implementing strategies and monitoring developments to mitigate risks and seize opportunities.

Brexit assurance

From a corporate governance and risk management perspective, businesses that have not done so already should carry out a Brexit assurance process (*see box "Brexit assurance process"*). This process is intended to ensure that a company's board can satisfy itself that all Brexit-related risks have been identified and, to the extent possible, that appropriate and timely steps are being taken to respond to them.

Planning for a no-deal Brexit scenario is the most effective way for businesses to compare their current position with a position in which the UK operates as a third country to the EU. Organisations can then see most clearly the impact of the possible changes and make a plan of action.

There is no one-size-fits-all process. Understanding sector-wide issues may assist but each business will need to identify its actual risks and solutions, which will depend on how the business is structured, how it operates and the details of its supply chains.

Ensuring continued supply

The key concern for most businesses will be ensuring that they are legally permitted to continue to supply their products and services, or can continue to be supplied with the products and services they need for their business, in the same markets after Brexit. After Brexit, both UK-based entities trading with the remaining EU27, and EU27-based entities trading with the UK, could find that they no longer have valid market access rights.

One example is the risk of financial services firms losing their passporting rights which enable them to provide financial services to clients in other EU member states on the basis of authorisation in one member state (*see Brexit sector briefing "Financial services and banking", www.practicallaw.com/7-638-0364*). However, other sectors face analogous issues. Broadcasters, for example, may lose the benefit of the country of origin principle in the Audiovisual Media Services Directive (*2010/13/EU*), which allows them to transmit freely throughout the EU so long as the business is licensed and regulated in any one member state.

In addition, certain products, such as medicines, require marketing authorisations issued by a body established within the EU. Similarly, manufacturers' or importers' licences may be required or the benefit of the mutual recognition of product standards or certification may be lost.

In order to maintain continuity, businesses may be able to:

- Establish a new legal presence and any necessary operations in the EU or the UK to obtain the required authorisations.
- Carry out an internal reorganisation, making use of the existing business footprint.
- Acquire entities or operations with the necessary legal presence or authorisations by way of strategic mergers and acquisitions.

Supply chain issues

There are particular risks for contracts that form part of a supply chain (*see feature article "Brexit and commercial contracts: assessing the impact", www.practicallaw.com/0-634-4336*). Steps to mitigate these risks include:

- Mapping supply chains, focusing on continuity of supply for any critical good or service. The most critical will not necessarily be the most valuable: it could be the hardest to replace and the problem may be below the first tier.
- Making enquiries of counterparties and key elements of the supply chain to ensure that they are proactively addressing Brexit risks.
- Considering the commercial impact of matters such as the impact in cost and delay on suppliers if they face the same import and export formalities imposed on trade from outside the EU, increased tariffs and changes in tax treatments (for example VAT), and the risk that key

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suppliers could fall into financial distress or crisis as a result of these changes.

Corporate restructuring

Establishing a new legal presence or moving operations to a different entity will have contractual consequences. For example:

- Moving a business from one regulatory environment to another will require a new regulator to approve a new suite of documents.
- Existing customer contracts may need to be migrated to the new entity.
- The new entity will need to benefit from third-party services and supply arrangements, whether existing or new.

Compliance with EU law

Obligations to comply with EU legislation may be affected by Brexit. It is not always obvious that some contracts may become non-compliant. For example, after Brexit:

- In the absence of any declaration of adequacy from the Commission, or other agreement with respect to the adequacy of data protection laws in the UK, EU data controllers will be in breach of the General Data Protection Regulation (*2016/679/EU*) rules if they transfer personal data to the UK without putting in place necessary arrangements to safeguard the personal data being transferred. One way to provide the appropriate safeguards will be for the EU exporting entity and the UK importing entity to enter into standard contractual clauses for non-EU jurisdictions approved by the Commission.
- English law governed contracts will become non-EEA law governed. Article 55 of the Bank Recovery and Resolution Directive (*2014/59/EU*) may therefore require EEA banks to insert clauses recognising the EU's bail-in powers into their UK contracts, unless otherwise agreed. UK regulators may insist on equivalent terms in contracts that UK banks enter into which are governed by the law of a jurisdiction within the EU27.

Repapering

If a business wishes to identify and implement changes to its contracts in preparation for Brexit, it may need to undertake a repapering project, that is, amending existing contracts. This could involve documenting the migration of contracts and necessary amendments as part of cross-border restructurings as well as parallel risk assessment exercises which involve locating, reviewing and amending contracts to ensure business continuity after Brexit.

While each repapering project will need to be tailored to the strategy of each business, it may involve the following phases:

Prioritising and planning. Businesses should invest time at the outset to agree a timetable and an overall project plan. They should also identify high legal risk contracts for initial sample review to identify key issues and solutions.

Reviewing and resolving. Businesses should identify the clauses that require amendment, analyse contractual permissions (for example, an ability to amend or transfer without third-party permissions) and analyse and identify practicable solutions to address regulatory requirements and constraints relating to transfers and amendments.

Drafting. New contractual wording may need to be prepared by way of, for example, new model clauses, standard-form variation agreements, toolkits or drafting and negotiation guidelines for existing and new contracts.

Implementing. Businesses may need to negotiate and apply drafting changes to the suite of documents.

The often high-volume, document-intensive nature of these processes lends itself to the use of technology and bulk document management techniques.

Contractual consequences

Brexit planning is likely to identify specific aspects of existing contracts that need to be risk assessed, amended or migrated to a different entity (*see box "Repapering"*). There will also be implications for new contracts being negotiated before Brexit to continue after Brexit.

Contracts may need to be amended to fix provisions which would otherwise become ineffective, uncertain or cause undesirable consequences after Brexit. New contracts may also need to take Brexit into account. For example:

- Definitions or clauses defined by reference to the EU will need to be amended as the UK will leave the EU on 29 March 2019 even if a transition period is agreed. This could include the territorial scope of a trademark licence that covers the EU, a restriction on transferring personal data outside of the EU or restrictive covenants applying in the EU.
- Contractual terms commonly include references to EU legislation (such as in relation to environmental matters and data protection rules) and will need to be able to be interpreted to include that EU legislation as incorporated into UK law.

Avoiding and resolving future disputes

Abruptly shifting regulatory environments and business models may require new dispute resolution strategies:

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- To deal with contracts that become legally difficult or uneconomic for any counterparty to perform.
- As part of contract renegotiation and repapering exercises that either the business or a counterparty has initiated.

Sometimes, a business may wish to bring contracts to an end due to difficulties in fulfilling its own obligations or to switch to alternative suppliers, or both. It may be possible, after careful consideration, to use the existing contractual framework, and other applicable law, to do so. For example, businesses may wish to consider:

- Terminating the contract in accordance with a termination clause (but loss of bargain damages will not typically be available where termination is under a contractual right rather than for repudiatory breach).
- Making use of a force majeure or material adverse change clause which may be triggered by a Brexit-related event.

Where a business is renegotiating or repapering its contracts, or entering into a new contract that will continue in force after Brexit, there may be an opportunity to introduce a Brexit clause to address future Brexit uncertainty. For example:

- A price adjustment clause which permits a supplier to adjust the price of goods to pass on changes to the costs of manufacturing and supplying the products. This could address who will be responsible for the payment of new tariffs (or who will benefit from the reduction of tariffs) imposed on the sale, licensing or transfer of goods or services between the UK and the EU.
- A right to renegotiate or terminate the contract on a specific event occurring when or after the UK leaves the EU. Specific triggers could include, for example, the loss of a necessary authorisation.

If considering using a Brexit clause, the triggers need to be considered carefully and would need to be sufficiently specific to be contractually enforceable.

Arbitration and Brexit

Brexit will not have any impact on arbitration or arbitration clauses in English law contracts. Arbitration is excluded from EU legislation regarding jurisdiction and enforcement, and a tribunal seated in London is not obliged to follow EU rules regarding choice of governing law. Therefore, following Brexit, an agreement to arbitrate in London and a resulting award will continue to be enforceable across the EU.

Governing law clauses

The continued operation within the EU of the Rome I Regulation (*593/2008/EC*) governing applicable law in contracts, and the Rome II Regulation (*864/2007/EC*) governing applicable law in tort, which (with some exceptions) give effect to a choice of law made by contracting parties, means that whatever law the parties have chosen, even if it is the law of a country outside the EU, will be applied. As such the validity and effectiveness of a contractual choice of law is expected to be unaffected by Brexit.

The question of whether the parties should continue to choose English law for their contracts will depend on the nature and purpose of the agreement. Many commercial parties choose English law as it is viewed as certain, stable and predictable, and generally gives effect to the parties' contractual bargain, thereby giving limited scope for implied terms or influence by public policy changes. This reasoning is unaffected by Brexit.

Jurisdiction clauses

The joint statement published on 19 June 2018 by the UK government negotiators and the EU negotiators outlining progress made on the draft withdrawal agreement since March 2018 confirms agreement in principle that the current rules (that is, the recast Brussels Regulation (*1215/2012/EU*) on jurisdiction and enforcement of judgments will continue to apply where proceedings were commenced before the end of the transition period. This will mean that, assuming that a transition period is agreed, in proceedings commenced before 31 December 2020 if the parties have included an English jurisdiction clause in their contract, the EU courts must defer to the English court if the clause is exclusive, or if it is non-exclusive and the English proceedings were commenced first. Therefore, English judgments will be relatively straightforward to enforce across the EU.

The position thereafter will depend on what, if anything, is agreed between the UK and the EU, including whether the UK is able to accede to the 2007 Lugano Convention. In any event, the UK intends to accede to the Hague Convention on Choice of Court Agreements, which it can do without the EU's agreement. Overall, it seems likely that most member states will continue to respect exclusive English jurisdiction agreements and enforce English judgments in most circumstances, but there are a number of areas of risk.

Whether contracting parties should continue to choose to have the English courts determine their disputes in these circumstances may depend on how important it is that a judgment will be enforceable in a member state (where there is any uncertainty as to the enforceability of English judgments in that member state under its national rules). That being said, the English courts still have a reputation for the quality and independence of the judiciary and for procedures that allow evidence to be tested thoroughly (*see feature article "International disputes in the UK: no cliff edge after Brexit", www.practicallaw.com/w-007-9799*). If a business's priority is a just result, the English courts remain a good option (*see also box "Arbitration and Brexit"*).

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