

# ALLEN & OVERY

An abstract graphic consisting of numerous thin, overlapping lines in shades of brown, grey, and black. The lines flow from the top left, curve downwards and to the right, and then spread out into a dense, swirling pattern that fills the bottom right portion of the page.

## **BREXIT LAW – FOUR CRUCIAL QUESTIONS**

*A long goodbye*

## Brexit – a long goodbye

*The process of unravelling the UK's 43-year-old relationship with the EU has only just begun, but it is already clear that it will be an immensely complex undertaking. It could be up to ten years before we have a proper picture of what the UK's changed position in the global economy looks like.*

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#### **BREXIT – A LONG GOODBYE**

The uncertainty unleashed by Brexit could be prolonged, perhaps lasting ten years. This is not a time for rushing into action.

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## Brexit – a long goodbye

*Wim Dejonghe and Andrew Ballheimer, A&O's senior and managing partners, reflect on the significant challenges that lie ahead for A&O and its clients in adjusting to the 'new normal' of Brexit.*

### THE UNEXPECTED LEAVE VOTE IN THE UK'S EU REFERENDUM

left many of A&O's clients reeling and in a state of shock, says senior partner Wim Dejonghe.

They are clear, like us, that a long period of uncertainty lies ahead while the precise terms of Brexit are worked out and negotiated.

"Companies hate uncertainty but they are now going through a very unsettling time that could endure for probably two to three years," he says. That timespan, he makes clear, is just to begin to see the shape of the new legal and economic landscape. The time it takes for the UK to actually exit the EU and put new independent trade agreements in place could take between five and ten years.

"It will take resilience. But companies just have to work out how this 'new normal' either hits their business or helps their business. Our role is to help clients find that new normal, to protect and guide them and to see where the opportunities are."

Managing partner Andrew Ballheimer agrees. "We are all working in a market that contains uncertainties and we just have to adapt to it. Whenever there is a shock to the system, the market has to find a new balance.

"Our system has endured global and regional shocks before, so you have to keep taking a long-term view and put today's situation in a historical context."

The firm and its clients must reflect and plan for the unexpected, Wim and Andrew agree. This is not the time to be rushed into action, particularly as the enormity of the political, economic and constitutional work that lies ahead becomes increasingly clear.

A&O did a huge amount of preparatory work in the run-up to the referendum to help clients assess the implications of the vote, whichever way it went. On the day of the result more than 2,000 client contacts around the world joined a briefing call with our specialist Brexit team. Many calls have been requested since, with clients joining from many different jurisdictions. And the library of briefings and advice notes on A&O's website continues to grow.

This supplement to our Annual Review forms part of our continuing efforts to work proactively with clients to chart a way through the current uncertainty.

In it we focus on four key legal issues: when the separation process should be triggered under Article 50 of the Treaty of Lisbon; the sort of exit deal the UK should be trying to negotiate; the process of renegotiating independent Free Trade Agreements; and the status of English law following the vote and following the UK's departure from the EU. We also asked three experts to sketch out some of the demands that might arise and the compromises that might have to be made.

"We hope this gives an indication of the scale and complexity of the challenges that have been unleashed by the 'leave' vote," says Wim. "It's a situation that will demand, from each of the negotiating parties, detailed thought, patient negotiation and careful political judgement."



# Article 50 – a very sensitive question of timing

*Deciding the optimum time to trigger the EU's separation procedures is an important issue. It's not a decision that the UK Government should want to rush. Moving too quickly may arguably not be in the EU's interest either.*

**THE UK'S DECISION TO LEAVE THE EU APPEARS TO BE SET IN STONE.** The new UK Prime Minister, Theresa May, made it clear as soon as she took office that “Brexit means Brexit”.

What remains unclear is how and when she will trigger Article 50 of the Lisbon Treaty, an article designed to start the formal two-year exit process.

Article 50 provides a framework for exit by a member state, but, as many now admit, it's not a provision anyone ever seriously thought would be invoked. As a result, the framework it provides is a high-level one, clearly neither precise nor detailed enough to cater for the scale of the constitutional and political changes that will arise from Brexit.

However, one thing the Treaty does make absolutely clear is that it is for the country intending to leave the EU, and for that country alone, to decide when to invoke Article 50.

Once the Article 50 notice is served, the UK's negotiating position is weakened. And whether the UK's negotiating position is stronger up until the trigger of Article 50 will largely depend on whether it will be possible to pre-agree on certain models. So far, there are limited indications that this will be the case.

## A QUESTION OF WHEN

At the end of the two-year period following the invocation of Article 50, if no exit deal has been reached (or no extension has been agreed by the remaining 27 member states) the UK will automatically leave the EU, through what we call the ‘trap door’ (or maybe the hangman's drop).

Some EU leaders have called for the UK to invoke Article 50 as soon as possible – anxious to limit the uncertainty that inevitably comes from a prolonged period of limbo.

Mrs May has already indicated that she will not serve Article 50 before the end of 2016, leading many to presume that she will probably do so sometime next spring. That would indicate the UK being out of the EU in early 2019, if the two-year timetable is adhered to.

Our view is that the process of unwinding the UK's 43-year relationship with the EU is something that may take between five and ten years to achieve, meaning it could take until 2026 for the UK and the remaining EU member states to learn the full implications of Brexit.

So the key question is: when in that continuum do you trigger the Article 50 process?

There are good arguments for the UK to take its time before serving the notice. If an exit deal is agreed prior to

the serving of Article 50, the two-year period that follows could be shortened.

If that timeline looks long, it's useful to remember that it takes up to four years to plan and execute the demerger of a typical listed company. Imagine, then, how long it will take to extract the world's fifth largest economy from the world's largest economic grouping – a demerger of staggering size and complexity.

## NEGOTIATIONS

Economically, politically and constitutionally this is a very difficult undertaking. The Article 50 notice is a key milestone.

If the UK serves the Article 50 notice early on – and without securing a thorough agreement on the principles underlying its exit terms – it could find itself walking away from the EU on terms that are largely unfavourable to the UK.

Once served, its EU partners may feel little compulsion to negotiate very much at all in the following two years – at which point the trap door would open, leaving the UK to drop out of the EU with little certainty about the way ahead. But whether there will be much enthusiasm within the 27 EU member states to negotiate ahead of the Article 50 notice is open to question.

Some EU leaders, notably French President François Hollande, have said there can be no negotiations before Article 50 is served. But German Chancellor Angela Merkel has taken a notably more conciliatory line, asking the UK to spell out what it wants to achieve.

## PASSPORT RIGHTS?

One reason why the City of London hopes the UK would have a detailed final deal in place before serving an Article 50 notice is that many financial services businesses rely on the single market ‘passport’, which allows them to sell services and products across the EU.

If the UK serves the notice without having retained the passport, those businesses are likely, at that point, to prepare for the worst-case scenario – no passport. That, in turn, would mean moving some or all of their UK operations to another EU27 member state – a process that could easily take two years or more.

They will have done the preparation (in fact we know they are doing contingency planning now). If the notice is served with no clarity regarding the passport, then – given the lead times involved – they are likely to push the button to move at that point. The assumption is that they will be gone, even if it ultimately transpires there was no need to move.

## CONSTITUTIONAL COMPLEXITY

We believe that the UK Government will want to begin the process of negotiating in the weeks and months ahead and, likewise, will want to avoid triggering Article 50 before a deal is agreed in principle. Whether that is a realistic expectation remains to be seen as it would depend on the UK and other EU member states being willing to begin early negotiations and reach an early agreement.

It is important that the UK and its EU partners do not underestimate the constitutional complexity of the process now

confronting the UK and the EU and the inadequacy of Article 50 to address that complexity. That ought to be a point of consensus.

### WHAT ROLE FOR THE UK PARLIAMENT?

One important question in the debate about timing is whether the UK Government can serve Article 50 unilaterally, using Royal Prerogative, or whether it will need to have the assent of Parliament. That issue is ultimately likely to be decided by the Supreme Court on appeal from hearings that will begin in October.

If the UK Parliament, which before the referendum had a strong majority in favour of remaining in the EU, is given the right to decide on when Article 50 is triggered, we would expect many members of parliament (MPs) to insist on it being done only when the UK has a clear view of the exit terms.

We expect that the UK Parliament is unlikely to block the exit process – even though, technically, the referendum result is only advisory. Neither the ruling Conservatives nor the Labour opposition appear to see any mileage in trying to reverse the referendum result, judging that it would be seen as a betrayal by ‘leave’ voters and anti-democratic.

But, equally, if Mrs May asks MPs to give her a free hand in the negotiations with the EU, she may well find they say no. She has only a slender overall majority in the House of Commons.

How long it will take to negotiate an agreement, and to subsequently win Parliamentary support for it, remains unclear.

But it is entirely possible to see a situation where Article 50 is not triggered until just before the next UK general election in, say, 2019, with Brexit taking place no earlier than 2021.

**“Economically, politically and constitutionally this is a very difficult undertaking. The Article 50 notice is a key milestone.”**

## What will the end deal be?

*The UK Government has been asked to spell out what it wants from Brexit negotiations. Work on that question has only just begun.*

**SO HOW WILL UK MINISTERS RESPOND TO CHANCELLOR MERKEL'S INVITATION** to spell out what the UK wants from the final Brexit deal? Again, there are different ways for the UK and EU to approach this conundrum.

The UK could present its partners with a short, one-page list of, say, five or six key demands, including, perhaps, access to the single market, controls on free movement of people, certain protections for the City of London and sovereignty.

Alternatively, the UK Government could opt, at the other extreme end of the spectrum, for a full legal agreement defining in detail the terms of the UK's exit and its future relationship with the EU.

This is unlikely to happen for a number of reasons, not least the fact that we do not see the UK and the EU27 member states agreeing to such an approach. We rather believe that there are merits to a pre-agreement on some underlying principles of the exit without getting into all the requisite detail.

But even in that case it would be a document running to many hundreds, if not thousands, of pages, covering a myriad of complex issues.

These would not only cover a holistic settlement on the key economic issues of free movement of goods, services and people and the future of the customs union, but also important constitutional issues, including: the relationship between the Republic of Ireland and Northern Ireland; the internal Irish border – the UK's only land border with the EU; and the status of Gibraltar, Scotland and Wales.

Getting agreement on specific market issues, such as the future of the proposed new Unified Patent Court and the terms on which international banks based in London can operate across the EU should their current passporting rights disappear, are among literally hundreds of issues that need to be resolved.

This process will take a long time to complete, not least because both sides start with pretty blank pieces of paper.

It's now abundantly clear that the UK Government did almost no contingency planning for a ‘leave’ vote, a fact that led the UK Parliament's Foreign Affairs Select Committee to accuse it of “gross negligence”, of deepening post-referendum economic uncertainty and of making the Brexit negotiations more difficult to conclude.

Even the cheerleaders of the ‘leave’ campaign emerged blinking on the day of the referendum result with, apparently, no clear ideas of the way forward.

That detailed work has now got underway with the formation of Theresa May's new Government. But it is a vast and lengthy exercise, not least as it involves considering hundreds of pieces of UK legislation which are currently tied to EU laws.

And it is an exercise that the UK is likely to want to complete before it triggers Article 50 if it is to mitigate the risk of falling through the trap door into an uncertain void.

# Free trade – the UK regaining the right to negotiate

*Putting comprehensive Free Trade Agreements in place will inevitably take time – especially with complex political and economic issues to reconcile.*

**AT THE HEART OF THE ‘LEAVE’ CAMPAIGN** was a vision of the UK standing on its own feet, successfully agreeing a host of independent trade deals with all the world’s most important economies.

The argument ran in the UK that the EU had always been an inefficient trade negotiator on behalf of its 28 member states and that, by going it alone, the UK could negotiate much better deals, much more quickly.

Dr Liam Fox, the UK Government’s international trade minister and a long-term advocate of Brexit, has argued that the UK could quickly tie up new trade deals, especially if the UK was to withdraw from the EU’s customs union.

In practice, that process is likely to be fraught with difficulty.

While still a member of the EU, the UK cannot even begin to discuss trade deals with any potential trading partner without being in breach of its Treaty obligations. This is because it has delegated its competence to negotiate deals under the World Trade Organization (WTO) umbrella to the EU.

Over the years, the EU has negotiated and concluded 53 trade agreements – with countries as diverse as Mexico, South Korea and Thailand – on behalf of its member states.

The UK will lose all 53 of those deals on leaving the EU and will have to renegotiate them from scratch, as well as trying to conclude new deals with other sought-after partners, such as the U.S., Canada and India.

This is a formidable and lengthy undertaking. Despite some arguing that deals could be put in place more quickly than in the past, it is instructive that Canada’s trade deal with the EU – itself potentially a good deal simpler than the one the UK may want to agree with the EU – has taken seven years to negotiate.

To begin freely negotiating new trade deals, the UK must first win back its rights to negotiate independently under the auspices of the WTO. If the EU does not agree to this, the UK may then have to approach the WTO to secure its blessing.

However, it’s conceivable that the WTO would refuse to talk to the UK while there was a danger of the UK being in breach of its Treaty obligations. We understand the WTO is currently considering the UK’s position as a potential member.

## A NEW RELATIONSHIP WITH THE EU – BREXIT LITE OR BREXIT HEAVY?

Two models for the UK’s future relationship with the EU are frequently cited – Norway and Canada. But neither would appear to satisfy the UK’s desire to remain an active participant in the EU single market.

Norway is outside the EU – a member, instead, of the European Economic Area (EEA) alongside Iceland and Liechtenstein, and a part of the European Free Trade Association (EFTA), which also includes Switzerland.

Norway participates fully in the single market but, in return, has to accept full free movement of goods, services and people and make contributions to the EU budget without having any representation on the EU’s decision-making bodies.

It’s clear that the UK Government would be unlikely to try to sell a deal to the UK electorate which involved free movement of people – it is one of the issues that they made clear they were most vexed about. That is likely to make the Norway model unworkable as far as the UK is concerned.

Canada’s EU trade agreement includes tariff-free access for manufactured goods, but less favourable terms for services. For an economy heavily reliant on its services sector, the UK would be unlikely to want to replicate such a deal.

The likelihood is that the UK will try to negotiate an entirely independent deal. Some have suggested that this could be ‘Norway-lite’ – with access to the single market safeguarded and with some limits agreed on the free movement of people, such as an emergency brake when levels of immigration reach an agreed level.

It was just such a deal on migration that former UK Prime Minister David Cameron sought to clinch ahead of the referendum. He was abruptly turned down.

Although such proposals may again be brought forward by the UK, it is unlikely that EU leaders would now be more willing to accept these requests. As some, including French President François Hollande and German Finance Minister Wolfgang Schäuble, have pointed out, access to the single market is unconditionally linked to free movement of people.

There may be one area of wriggle room, however. The UK, like other EU member states, remains a ‘contracting party’ to the EEA. Some have assumed that the UK, once it drops out of the EU, would also automatically drop out of the EEA.

However, the EEA Treaty has its own exit provisions – Article 127 – under which members are given a year to withdraw. The UK might, in theory, be able to remain a contracting party to the EEA – perhaps as a stopgap while it renegotiates its competence with the WTO to sign its own Free Trade Agreements.

This would also mean it could still benefit from key elements of the EEA agreement, such as the rules on free movement of goods, but would no longer be subject to rules on free movement of people, because it is neither an EU nor an EFTA member state.

This could buy the UK some time and leave it with one strong card to play in an otherwise rather uninspiring hand.

# English law and the English courts – resilient or diminished?

*English law and the English courts will remain attractive choices for commercial parties post-Brexit in all but a few cases.*

## **SOME HAVE USED THE BREXIT DECISION AS AN OPPORTUNITY**

to argue that English law is now a broken system and that the English courts are courts that investors and commercial parties will want to steer clear of.

There is in fact no evidence to suggest that this is the case. Nor is there any reason to suggest that New York or Delaware law or courts, or continental European laws or courts, have a significant advantage over the English system that did not previously exist, particularly in the context of international transactions and in the financial markets.

Such statements are much more a reflection of the high levels of competition between different governing legal systems (and the law firms that service the work) – a competitive landscape that is delivering, and that will continue to deliver, real benefits to commercial parties.

English law – like New York law – is popular in jurisdictions around the world, including across Europe, Africa and Asia, for very practical reasons.

Parties choose English law because it is a well known system that delivers predictable results, based on a huge body of precedent. It is also valued because contracts tend to be interpreted literally – something business people really appreciate. It is also widely used because it is highly flexible, allowing parties to use innovative structures in deals and contracts.

These reasons for choosing English law are unaffected by Brexit, at least where contracts between commercial parties are concerned.

We believe English law will therefore remain a popular choice for commercial parties in all but a very few cases (for instance, in the narrow category of cases where certain European regulations stipulate the use of a member state law).

There is also little chance, we believe, that a choice of English law will be any less respected by courts in the EU once the UK leaves.

As for the English courts, they have always proved popular among commercial parties as the chosen jurisdiction for settling disputes for very straightforward reasons.

They are seen as independent, to have vast experience in adjudicating complex cases and to have a strong system of precedent. They are also widely recognised as effective by the financial markets. In particular, a ‘foreign’ litigant can have comfort that English judges will not favour a ‘home state’ litigant, if there is one, and the English courts are seen as creditor-friendly, something which financial institutions value highly. None of these reasons for choosing to resolve disputes in the English courts will be affected by Brexit.

The enforcement of English court judgments in EU states is going to be less straightforward after Brexit, as English judgments are currently enforced under simplified EU mutual recognition rules.

It is likely that the UK would fall out of this regime on Brexit and it remains unclear what regime will be put in its place.

But that does not mean that English judgments will be unenforceable in the EU after Brexit. In fact it is likely that in most cases it will still be possible to enforce English judgments, although it will probably be more time-consuming and costly to do so.

Consequently, we do not expect Brexit to make a significant overall difference to the popularity of the English courts.

Of course the most important point for commercial parties – both in choosing a governing law and specifying which courts will have jurisdiction – is one that has always applied. Parties should choose the option that best suits the deal being done.

**“We believe English law will therefore remain a popular choice for commercial parties in all but a very few cases.”**



**JOSH HARDIE**

Deputy Director-General of Policy and Campaigns at the CBI

## UK business must help shape Brexit

*As creators of jobs and prosperity, businesses with UK operations want clarity and a role in shaping the Brexit negotiations, says Josh Hardie. They have five key priorities.*

### Choosing directions

*Brexit will mean taking account of many different interests – political, economic and commercial. We asked three experts to sketch out some of the demands that might arise and the compromises that might have to be made.*

#### **BUSINESSES ARE THE CREATORS OF JOBS AND PROSPERITY**

and responsible for building relationships and trade with partners all over the world. They, therefore, have a fundamental role to play in shaping the UK's forthcoming negotiations with the EU.

Businesses across the UK are stepping up to the challenge and they are well placed to do so – they are used to dealing with change and uncertainty, assessing opportunities while continuing to serve their customers.

To help them play their part, the Confederation of British Industry (CBI) has called for a new partnership between the UK Government and firms of all sizes.

Businesses with operations in the UK are determined to speak with as unified a voice as possible to help government understand the key priorities for renegotiation. In return, business also wants this same clarity from government and a proper plan for the country's future economic relationships.

To support this conversation, the CBI has surveyed more than 500 of its members. While opinions vary between businesses, five clear principles have emerged that they regard as key to future negotiations.

Top of the list comes the clear call: the UK must continue trading easily with its neighbours. With 45% of the UK's exports destined for the EU, alongside 53% of imports, maintaining easy access to this market is a major business concern.

The level of access to the single market has implications for people's ability to live and work across the EU: there are genuine concerns over immigration. To thrive and grow, business also needs access to talent from across the world.

Despite historically high employment, companies still struggle to fill positions in certain sectors. And although it is vital for the UK to upskill its domestic workforce, free movement from the EU has helped companies overcome these shortages.

This is not simply a long-term challenge. It is an immediate and real concern for EU migrants already in the country – and UK citizens resident in the EU – who urgently need clarification about their status once the UK has left the EU.



Our members also highlight the need to strike a balance between UK- and EU-led regulation in the future. In areas where the EU currently facilitates international collaboration – including aviation and medical licences – we still need to be involved. And we need influence over new EU rules and standards that may still apply to the UK’s trading businesses post-Brexit.

The possibilities for new trade deals with established and growing markets are exciting. But the EU’s trade deals with third-party countries have already helped to bring barriers down. CBI members are clear they want to protect preferential access to markets through these deals.

Finally, businesses that have matched EU investment in projects that support infrastructure, small and medium enterprises, research and innovation, and the rural economy are in need of urgent assurances that funding promises will be honoured.

Managing these priorities will be a balancing act. But at the root of them all is a simple message: a new era of partnership is needed so that businesses have the right foundations to continue creating prosperity, for the benefit of all.

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Josh joined the CBI as Deputy Director-General, Policy and Campaigns in March 2016. Prior to this, he was Group Director for Corporate Responsibility at Tesco, leading the integration of social and reputational issues into business strategy and developing a new approach to campaigning on issues including health, employability and sustainability. Josh has held director-level roles at EdComs Ltd – a leading communications and CSR agency – creating campaigns for clients including Google, the NSPCC and the British Army.

## “Could the EEA Agreement be used by the UK as an interim step on the way out of both the EU and the single market, rather than on the way in?”

*Sebastian Remøy*



**SEBASTIAN REMØY**

Global Head of Public Affairs for Kreab

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## Norway, Switzerland, bespoke-UK – no option looks easy

*The UK faces a stark choice – a solution that works economically, or one that works politically, says Sebastian Remøy. It can't have both.*

**THE UK FACES SOME EXTREMELY DIFFICULT CHOICES** as it tries to put its relationship with the EU on a new footing post-Brexit.

There’s little agreement on which existing model, if any, the UK should follow as it tries to cement this new relationship.

But some suggest it will involve signing up, if only temporarily, to the EEA, as Norway, Iceland and Liechtenstein have done.

So it’s worth understanding the EEA Agreement in a little more depth – the benefits it provides and the obligations it places on a country like Norway.

As the Agreement was being drafted, due to its obvious democratic deficit, it became apparent that it was most likely to serve as a stopgap, a plan B. During the latter stages of its negotiation it was viewed as an interim step on the way to Norway and other countries becoming full EU members, an option that Norway ultimately rejected.

The question now is: could the EEA Agreement be used by the UK as an interim step on the way out of both the EU and the single market, rather than on the way in? Possibly, but that would mean squaring some awkward circles.

Firstly, it would mean continuing to adopt EU regulations. Norway adopts several hundred pieces of EU legislation every year. Or, by some estimates, for every day the Norwegian Parliament sits – a five-a-day diet, courtesy of Brussels.

But, with practically no representation and no vote in all the major EU institutions, Norway cannot decide the legislation and has very limited powers to amend it. It accepts this situation as the price to pay for full access to the single market.

Norway benefits from the fact that the relevant laws are ‘regularly upgraded’ and kept relevant when they change (something that does not happen within Switzerland’s non-EEA relationship with the EU, which is based, instead, on bilateral treaties).

Under the EEA Agreement, EU budget contributions also continue. Norway pays some EUR800 million into the EU budget each year.



Norway also buys into the homogeneity of the single market project, accepting all four of the pivotal freedoms: free movement of goods, capital, services and people – the last of which is as inviolable as the rest.

Free movement of people is important to Norway. A number of key sectors, including farming, fisheries, oil and gas, and Oslo's strong services sector, rely on it.

The conditions of the EEA Agreement would provide the UK with a sought-after economic benefit: continued access to the single market.

But these conditions clearly present political hurdles that would be hard to overcome for British pro-Brexit campaigners. Sovereignty, taking back control of EU budget contributions and ending free movement of people were all, variously, at the top of the 'leave' campaign's agenda.

And it's not a one-way street. Key political figures in Oslo have questioned the advisability of the UK's presence in the EEA as an EFTA state, and whether that would be a positive thing for Norway. Other EFTA states would also be keen to ensure UK re-entry would not harm their interests. Some appear slightly more positive than others, but any one of the four could block the UK. It is not inconceivable, however, that all EFTA countries could bow to pressure to accept the UK back into the club if that was deemed overwhelmingly to be the best solution by major partners in Europe and the international community. But then there is the question of UK re-entry into the EEA. All 30 EEA states (27 from the EU and three from the EFTA) would have to consent to that.

Emulating Switzerland's arrangements with the EU – based on bilateral treaties – presents problems too, which could soon come to a head after the Swiss people voted, in 2014, to end the free movement of people. If the two sides cannot resolve this issue by the February 2017 deadline, it could mean that Switzerland's already limited access to the single market might no longer be guaranteed.

Under the Swiss model, there is no structure for regular updates of legislation to ensure homogeneity between Switzerland and the EU. This can be restrictive for some Swiss companies wishing to trade in the EU. The contrast with the EEA Agreement is stark. The EEA is referred to as a dynamic agreement (the only example). It has special institutions corresponding to the Commission and the European Court of Justice that promote the homogenous and simultaneous implementation of internal market rules. Because there is no similar two-pillar structure for the Swiss agreements, and because in contrast to the EEA Agreement they are not updated on an almost monthly basis, Switzerland's agreements with the EU are characterised as static. British businesses would be much better served by a dynamic agreement with the EU as it secures, to a much higher degree, unimpeded and uninterrupted access to the single market.

The limitations associated with both the EEA and Swiss options lead many to believe that the UK will push for a bespoke settlement. One suggested outline of such a deal is that the UK would retain access to the single market but be granted an emergency brake on EU migration.

Currently, such a deal looks like the product of some wishful thinking. Yes, some do suggest that EU member states might be

flexible on this, but there are just as many for whom tampering with free movement would destroy the homogeneity principle of the single market.

And remember, any such bespoke agreement will likely have to be ratified, not just by member states, but by the European Parliament too, and possibly also national parliaments. Even if the negotiations go more smoothly than expected, any agreement could be unravelled in the ratification process.

So the UK's dilemma would seem to boil down to this. It can have a good economic result, or it can have a good political result. But it can't have both.

If you want to keep the economic side happy, then you have to compromise politically.

At this stage it's not easy to see if and how that compromise can be made.

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**CHARLES GRANT**  
Director of the Centre for European Reform

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## A complex web of deals

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*Charles Grant explains the complex set of negotiations that will happen following the Brexit vote, arguing they will take much longer and be far more complicated than many British politicians realise.*

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**BRITAIN'S EXIT FROM THE EU** will require not just a single deal, but at least six interlocking sets of negotiations, each highly complex in their own way.

The first deal – the divorce settlement prescribed by Article 50 – will divide up the properties, institutions and pension rights, and deal with budget payments. It will also cover the rights of UK citizens in the EU and vice versa.

The Treaty on European Union sets out a two-year period for this negotiation, extendable by unanimity. But the 27 other EU member states are unlikely to extend and many may want

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## SIX DEALS THAT NEED TO BE DONE

- Article 50
  - A new UK/EU trade deal
  - An interim (possibly EEA) agreement
  - The UK and the WTO
  - New bilateral trade deals internationally
  - An EU/UK agreement on defence and security
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Britain out before the June 2019 European elections, and before talks on the EU's next seven-year budget cycle get underway (the current cycle ends in 2020).

The second deal will decide what shape a Free Trade Agreement (FTA) with the EU will take.

It could be similar in scope to Canada's recently negotiated FTA with the EU, not least because the much-discussed 'Norwegian model' looks increasingly unviable as an alternative.

Norway, as part of the EEA, participates in the single market, but pays into the EU budget and has to accept free movement of people. The latter condition, and perhaps the former, is likely to be unacceptable to the British Parliament following the referendum result.

But even a Canadian-style FTA will require the British Government to make significant trade-offs. Such a deal may eliminate tariffs on manufactured goods – but only if the UK agrees to comply with key EU regulations.

And it would probably only guarantee limited access to the single market for services, with negative impacts not just for financial firms but for other sectors such as tourism, accountancy, law and air transport.

Whether talks on the deal start before or after the UK has left the EU, it's clear that the FTA will take many years to negotiate and ratify and that there will be a significant gap between Britain leaving the EU and the FTA coming into effect.

That calls for a third, interim deal. One possible interim solution would be for the UK to become an EEA country for a limited period, while FTA talks proceed. But that would involve the UK accepting substantial EU budget payments, free movement of labour, and most of the EU's single market rules. Furthermore, the existing EEA countries show little desire to reconstruct their own treaties and institutions to accommodate the UK as a temporary visitor.

The fourth deal involves the UK attaining full WTO membership. Britain is currently a member via the EU. There are huge complications here, not least the fact that any deal requires the approval of all the other 163 WTO members. Although British officials hope this can be achieved, they recognise it will be hard to sort out WTO membership within the two years of the Article 50 negotiation.

The fifth negotiation concerns the series of deals that must be struck with the 53 countries that have FTAs with the EU. Here the legal position is that the FTAs cease to apply on the day that Britain leaves the EU. The UK will have to quickly cut its own bilateral deals with these countries, before that exit date. While most of the 53 will probably try to be helpful, some may have competitive reasons to be more difficult.

Striking new deals with countries that have not yet agreed an FTA with the EU – such as the U.S., China, Australia and New Zealand – will be also be tricky, legally and practically.

So long as the UK is part of the EU, it cannot legally complete an FTA with another country. It can only talk about talks. But given that its current capacity for trade negotiations is stretched, it is likely to prioritise the EU FTA and securing bilateral deals with the 53 countries.

In any case, it's difficult to see why countries like the U.S., New Zealand or China would want to negotiate an FTA with the UK before knowing answers to some pretty fundamental questions, such as: Which bits of the single market, if any, will the UK be in? And which parts of EU competition law will apply to the UK?

The sixth negotiation will cover UK/EU ties in areas like foreign and defence policy, police and judicial cooperation and counter-terrorism. Here, the UK is in a relatively strong position. It has important diplomatic, intelligence and military assets that can be useful to its partners.

As we wait for these negotiations to get underway, one thing seems pretty clear. The other 27 EU member states are likely to take a much tougher line than some in the UK expect.

Brexit and the rise of populist anti-EU movements in some member states may have changed the political climate and have certainly weakened those pursuing a federalist agenda.

But European leaders are unlikely to compromise on fundamental single market principles, such as free movement of people. And they will not want the process of Brexit to be painless – not least as it will deter others from trying to follow the UK's example.

The diplomatic endeavour involved in completing these negotiations is clearly immense.

If Theresa May's Government believes it is important to reach a conclusion quickly to limit economic uncertainty, there will be a strong incentive, and considerable pressure, to compromise.

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Charles helped to found the Centre for European Reform (CER) in 1996. In January 1998 he became the CER's first director. He is the author of numerous CER publications, including *Russia, China and Global Governance* (2012) and *How to Build a Modern European Union* (2013). His specialisms include EU foreign and defence policy, Russia, China, the euro and global governance. He is a member of the councils of the Moscow School of Civic Education, the Turkish think-tank EDAM and the French think-tank Terra Nova.

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The implications of the UK vote to leave the EU are changing on a daily basis; the content of this publication was prepared on the basis of the legal, political and economic situation in mid-August 2016.

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