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PERSPECTIVE

Key issues for US firms to know about UK decision to Brexit

By Stephen Gillespie

On June 23, the U.K. electorate voted to leave the European Union. On June 24, British Prime Minister David Cameron announced that he would step down as leader of the Conservative Party and prime minister once a new leader of the Conservative Party had been elected, which he expected would happen before October 2016, and that the U.K.'s exit negotiations with the EU should be handled by his successor.

Has Anything Changed Since June 23?

The referendum vote is not legally binding on the U.K. government. Until the U.K. leaves the EU, it will remain an EU member and all EU law will remain in force in the U.K. Notwithstanding continuing market volatility and political uncertainty, it is "business as usual" when it comes to doing business with and in the U.K. and the EU.

Care should be exercised when entering into any transaction or arrangement with a U.K. or EU entity and/or which is governed by U.K. law and/or in monitoring existing transactions and arrangements with U.K. and EU entities.

Some issues should be considered now:

Favorable treatment under EU Law: In a worst-case scenario, it would be prudent to assume that EU law, which is now part of U.K. law, may not be as of Brexit. If any particular transaction or arrangement relies upon a particular treatment or outcome (such as, for example, favorable tax, IP or free trade treatment) by virtue of the provisions of EU regulations or U.K. law giving effect to EU directives, care should be taken to consider the consequences if, following exit, those regulations or laws cease to have effect in the U.K.

Future incompatibility with EU law: Similarly, consideration should be given to any obligation or condition which, post-exit, could be at odds with or in breach of EU law even if it was compliant with the provisions of U.K. law following exit.

Asset valuations and margin calls: Continuing market volatility (in particular, currency fluctuations and the fall in value of listed securities) could give rise to asset valuation issues — specifically, the value of collateral supporting margin loans and other collateral-linked facilities. Beware of possible margin calls, and give consideration to implementing hedging arrangements to mitigate volatility.

EU-wide licensing: In the case of businesses which are reliant on EU-wide regulation or licensing (such as the medicines and life sciences industries, and energy, roads and transportation), consideration should be given to the consequences of there being no agency or entity post-exit which was able to provide the agency approvals currently enjoyed.

Freedom of movement and employment: Businesses which are reliant on the free movement of EU citizens for the employment of non-U.K. nationals in the U.K. (or vice versa) should consider the implications of freedom of movement being removed post-Brexit. Such businesses could find themselves in a position where some of their employees were not legally entitled to remain in the U.K./EU. We anticipate the implementation of transitional arrangements to mitigate any problems which might otherwise arise, but this is an area that should be carefully monitored.

Fundraising and AIFMD: The U.K.'s status under the Alternative Investment Fund Managers Directive will depend upon the U.K./EU post-exit model. Absent transitional arrangements, were the U.K. to separate entirely from the EU and not remain in the European Economic Area, then it would become a "third country" for AIFMD purposes and the marketing passport into Europe would no longer be available to U.K.-authorized funds. Any U.K.-authorized fund manager considering a European fundraising might seek to ensure that that fundraising is implemented before a U.K./EU separation to benefit from the passporting and other freedoms enabled by AIFMD. Equally, and any manager which is considering being authorized in Europe may want to carefully consider which EU jurisdiction they want to be authorized in in order to benefit from the passporting and other freedoms under AIFMD.

Fundraising and capital markets: Similar passporting issues arise in relation to the public offering of securities in the EU. Currently, once a prospectus in relation to an offer to the public of debt or equity securities has been approved by a single EU member state, that prospectus can be used to offer such securities throughout the EU in accordance with the EU Prospectus Directive. It may be prudent to consider the timing of any prospective public offering of debt or equity securities to take advantage of the favorable passporting arrangements which currently apply.

What Next?

Cameron's June 24 announcement means that a U.K. government will not invoke the EU exit mechanisms until a new prime minister is installed. That process will be completed by no later than Sept. 9, 2016.

The referendum result is advisory and does not tie the U.K. government to any particular course of action. It is a political judgment for the government of the day as to whether it acts upon or ignores the outcome of the referendum. It is inconceivable that the new prime minister will ignore the outcome of the referendum, and probable that the government will seek to give it binding legal effect and will take the view that it requires some form of parliamentary approval to commit the U.K. to Brexit.

Timing

The delay to September/October 2016 implicit in Cameron's June 24 announcement has met with disapproval — the EU has insisted that exit negotiations should start as soon as possible, as have many of those who supported the "remain" campaign. There is a legitimate view that continuing uncertainty is destabilizing and bad for financial markets and investor confidence and, therefore, undesirable.

There has been a softening of tone from the EU, with the French and German governments recognizing that it is for the U.K. to initiate the exit procedures and the U.K.'s exit negotiations cannot begin until a new government has been installed.

In the meantime, the U.K. government has formed a team to begin addressing exit issues and preparing for an exit negotiation, and there will be continuing contact between the U.K. government and the institutions of the EU in preparation for a formal exit negotiation starting sometime in the autumn of 2016.

It is our view that the U.K. will not leave the EU before late 2018 or, more likely, early 2019.

Can the Referendum Result Be Reversed, Ignored or Blocked?

In spite of popular protests, there is no constitutional basis on which a second referendum on the same question could be held, and, currently, no political will to do so. Any U.K. government wishing to give binding legal effect to the referendum vote would almost certainly want to secure a parliamentary majority on a resolution to do so. Around three quarters

of MP are supposedly in favour of remaining in the EU, and so a government seeking a parliamentary mandate for exit could struggle to achieve the (simple) majority required.

An alternative would be for the incoming government to call a general election to secure an electoral mandate for exit. The U.K. parliament can only be dissolved ahead of its five year fixed term if the government loses a "no confidence" vote, or a two-thirds majority of the House of Commons votes in favour. It is conceivable that the incumbent government could make a vote on a Brexit resolution a "confidence" vote such that its loss would trigger dissolution of and a general election.

A third possible outcome would be for a second referendum to be held at the end of the exit negotiations in which the U.K. government would put to the U.K. electorate the question whether the country should rejoin the EU on whatever revised terms had emerged from the exit negotiations. It is being suggested that this is a plausible scenario in two or three years' time. In the meantime, the referendum result is neither going to be ignored nor reversed, so the U.K. will continue on a path towards an eventual exit from the EU.

There are, therefore, some complex political calculations to be weighed, and some practical hurdles to be overcome, before formal exit negotiations are commenced, all of which add to the view that such negotiations may not be formally initiated before the end of 2016.

Longer-Term Legal Consequences

The U.K.'s trajectory towards Brexit gives rise to potential legal issues in many areas. At this stage, however, there is so much uncertainty around what a post-Brexit world will look like that it is difficult to be specific about mitigating steps that can be taken pending a clearer picture emerging or to make recommendations beyond the practical steps outlined above.



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