

Brexit basics

The Four Freedoms

KPMG International

“Brexit means Brexit”. The UK plans on leaving the EU — and rescinding its membership of the Single Market and the EU customs union. No longer bound by the Four Freedoms, this ‘Brexit’ will mean a change to the relationship between not only the EU and the UK, but also the trading arrangements between the UK and the rest of the world. So **how will the free movement of goods, services, capital and people change post-Brexit?**

What are the Four Freedoms?

They are the four pillars to EU integration. Whilst some are said to be more ‘free’ than others in practice, trade under these principles is relatively frictionless for business within EU countries, particularly when compared to the rest of the world operating under free trade agreements (FTAs) or World Trade Organization (WTO) rules.

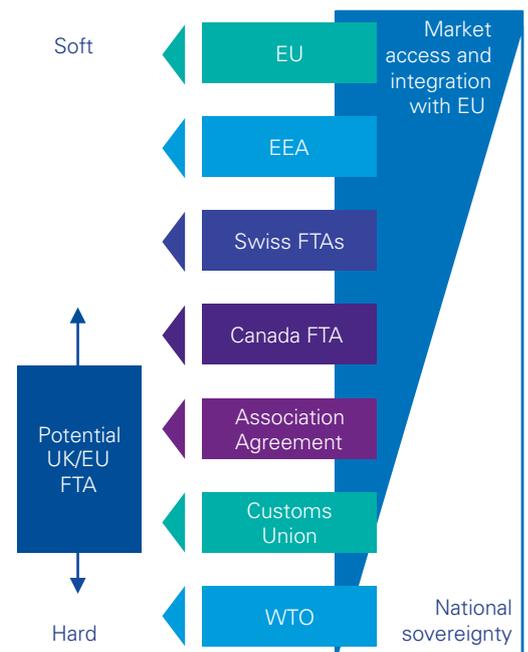
Free movement of goods	Freedom of establishment and freedom to provide services	Free movement of capital	Free movement of workers
This can be thought of in two ways: tariff-free access to the single market and the elimination of non-tariff barriers such as product regulation and approvals.	This means that once a company is established in one EU country it can sell services into other EU countries, without needing to establish a branch or subsidiary there. This is also known as ‘passporting’.	This is an important component in cross-border transactions and investments, ensuring few restrictions or capital controls on moving funds between member states.	Although the freedom is described as relating to workers, in practical terms this includes family members and those seeking work. It is often therefore described as free movement of people.

What will this look like post-Brexit?

In simple terms, the negotiations will be defined by the trade-off between the four pillars i.e. what extent of restriction on one freedom can be traded for concession on another. This is at the crux of the negotiations between the UK and the EU.

Membership of the EU Single Market and customs union is necessary to retain the same liberalized movement of goods, services and capital. The UK has indicated that it will rescind its membership, and instead is seeking a bespoke deal (FTA) that would retain the “greatest possible access”, but sever ties to the free movement of people. But no ‘off-the-shelf’ model allows for a similar freedom of trade without free movement of people. Whilst comprehensive, the Canada-EU FTA allows for less ‘free’ access than full membership, particularly in relation to services and capital, whilst the customs union with Turkey requires customs checks and restricts its independent trade policy.

‘Bargaining chips’ may be traded to retain freedoms for prioritized sectors, such as the continued cooperation of the UK in European security and intelligence, but these are far from certain. Any concessions will be in inherently political and subject to the whims of the UK and EU electorates, which have so far proven to be unforgiving in their own ways.



What does this mean for businesses?

It would be perilous at this stage to predict the relative winners and losers across the four freedoms. Immigration is the UK government's red line, so a reasonable planning hypothesis might be 'what extent of single market access could our business be faced with, for a given level of immigration'. This clearly has many permutations, but it reduces the number of variables you might consider.

'Optionality' is the mantra you may well live by in these uncertain times. For some, that means freezing hiring in London and recruiting people elsewhere. For others, it means diversifying the suppliers of critical components in the supply chain. This might be the cost of uncertainty you have to bear now to retain the widest range of options when things become clear(er).

Those more comfortable with ambiguity may want to continue to wait and see before acting. Either way, here are the broad-brush business implications of the Four Freedoms under different scenarios and the things to watch in the negotiations.

How a change in the freedoms will affect businesses

What to watch out for in the negotiations

Goods

The introduction of barriers to trade will increase costs, complicate decision-making, and may result in other countries and trading partners gaining competitive ground. But this is not insurmountable — a large amount of global trade takes place without an FTA, under WTO rules.

- BESPOKE: Tailored customs agreement with zero tariffs, EU-UK FTA with mutual recognition of controls/standards, agreed definitions, origin rules allowing for expedited movement
- WTO: Acceptance of UK schedules, including split of EU/UK WTO tariff quotas and subsidy caps
- Bilateral FTAs with other major trading partners

Services

The impact will depend on trading terms imposed on the modes of supply (including cross-border and commercial presence) and the proportion of business conducted into/out of the UK. Firms may need to restructure operations or establish separate entities to continue to do business in the UK or EU.

- BESPOKE: FTA with retained freedoms and/or regulatory equivalence for prioritized sectors, mutual recognition of qualifications, registration and licensing
- WTO: WTO General Agreement on Trade in Services (GATS) terms
- Bilateral FTAs with other major trading partners

Capital

'Brexit' may require detangling the highly integrated UK and EU capital markets — a costly and lengthy process. An extended period of uncertainty, loss of economies of scale or a shift away from harmonized regulation may lower investment activity and increase the cost to do business in the UK and the EU.

- BESPOKE: Retained freedoms and/or regulatory equivalence for prioritized sectors
- WTO: Liberalization of capital through extensive bilateral FTAs

People

Loss of free movement will likely result in increased compliance costs and delays for cross-border workers. Imposition of immigration quotas (EU or otherwise) may make it difficult to attract and retain highly skilled workers in UK operations — from which other countries and companies may benefit.

- BESPOKE: Repatriated control over immigration
- WTO: Movement of highly skilled talent to/from the UK in targeted sectors as part of other FTAs

The Four Freedoms will be less free, and that is simply the new operating reality. Immigration in the UK will be restricted, so you may want to start with contingency planning for your workforce now. Indirect taxes is an area with extensive global precedent, so you may choose to back yourself to deal with that on the fly. In any event, checking your organization's agility and resilience to change is a worthwhile investment of time and effort, now.

So what should you be thinking about?

Whether it be risk or opportunity, think about your business in the context of the Four Freedoms, and ask what strengths and weaknesses do geopolitical shocks — like Brexit — expose in your business and operating models. Looking at your business through KPMG's framework of 9 Levers of Value, you may ask the following questions:

A change to the movement of goods may impact on:



Clients and channels: *How resilient is your business to the loss of a key customer? Are your UK or EU customers already developing alternative suppliers? Will you need to review pricing policy for changes in tax or costs?*



Branding and markets: *Is there an open window of opportunity for foreign brands if British brands face negative sentiment from EU consumers if discussions become tense? What mitigation strategies exist? Which alternative markets and new trade routes should be explored? Will trade between the EU and UK reduce? Will trade with countries where the EU has FTAs be affected?*



Core business processes: *Will you need to review your 'go to market' approach? Does your distribution footprint and network still make sense in light of major geopolitical changes? Do you have enough visibility over your supply chain to identify threats? Do you have natural hedges?*



Measures and incentives: *Do you have sufficient data to understand how resilient your business is? How can you improve monitoring to identify any shocks early? Have you quantified the potential changes to the effective tax rate?*

A loss of movement of services could impact on:



Organizational structure, governance and risk: *Will your corporate structure need to change to take advantage of opportunities? Or respond to changes in regulation? If you restructure your organization in the UK or rest of Europe, will you face exit tax costs on transition?*



Operational and technology infrastructure: *Will restrictions on cross border activity increase the administration burden for your global operations? Will IT systems need to be adapted? Are your systems and processes set up for increased logistics, tax impacts or new pricing structures?*

Restrictions on the free movement of capital could impact on:



Financial ambitions: *What does potential uncertainty mean for availability and cost of capital? Will investors continue to fund capital investment programs? Will you update your forecasts in light of new economic scenarios?*

A change to the movement of people may impact on:



Organizational structure, governance and risk: *Can you manage your business if you face travel restrictions?*



People and culture: *How do you manage your global workforce and the restrictions that may come on them? How will you meet the gap when non-EU immigration is also restricted? How will your workforce change? Or your organizational culture? How will you deal with employment policies in UK or European operations after Brexit? How will you deal with racism/xenophobia if they raise their ugly heads near you?*

It is not about having the right answers, right now. The next best thing to having all the right answers is being able to ask the right questions. Think through the possibilities, and prepare your organization to respond to the signals of major change in this increasingly Volatile, Uncertain, Complex and Ambiguous (VUCA) world.

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