

Brexit basics

What 2017 holds for Brexit

KPMG International

Every day brings new dimensions to Brexit, not least from the political changes in the EU - like the Italian referendum, Austrian election, resignation of the President of the EU Parliament etc. The UK may have indicated that it will rescind its membership of some EU institutions, but there is a lot still to be determined on the terms of the UK's departure and its future relationship with the EU. With all this noise, it can be hard to follow the debate. **So what does 2017 hold for Brexit?** Let's take a look at the timeline and processes ahead.

What needs to be negotiated?

The referendum may have been phrased as a simple 'yes' or 'no', but Brexit will not be a two-sided negotiating process with a straightforward 'leave the EU' mandate. There are five key components to the task facing the UK.

Withdrawal

Article 50 provides for an agreement that *sets out the arrangements for the UK's withdrawal, taking account of the framework for its future relationship with the EU*. It is likely the 'divorce' will cover immediate issues — such as the rights of nationals, EU agencies, and justice and security. What falls into the 'remarriage' is not specified, and the negotiations may or may not occur in parallel. Why does that matter? In one word — voting. The 'divorce' will be determined by an enhanced qualified majority vote in the Council of the EU and EU Parliament. Voting over any future arrangement between the EU and the UK will be dependent on the policy areas covered. A comprehensive agreement encompassing 'shared' competences — such as that sought by the UK — will likely require ratification by national and regional Parliaments of EU member states — which may result in blockades and delays.

EU-UK relationship

UK regulation

Not only does EU regulation need to be enacted into domestic UK law (to prevent gaps and allow the UK to 'localize' it), but some of the 'competences' being returned to the UK will be returned to the devolved governments of England, Northern Ireland, Scotland and Wales — and with it, the possibility of regulatory divergence and barriers to business across the UK.

World Trade Organization

The UK is a member of the WTO in its own right, but the rules (schedules) are currently set by the EU. The UK will be required to negotiate its own terms of market access for goods and services (such as the split in tariff rate quotas) and subsidy limits with the EU, to be agreed to by all 164 members.

UK — rest of the world

The UK will likely lose access to the FTAs concluded or being negotiated by the EU — with around 47 percent of exports in a potentially less advantageous arrangement. But the UK will have the freedom to negotiate new deals — although formal conclusion will have to wait until its exit (and likely after WTO terms are agreed).

The UK has indicated that it will rescind its membership of the EU Single Market and customs union, but seek a comprehensive Free Trade Agreement and customs arrangement with a transitional period. However, the UK Prime Minister has stated that “no deal is better than a bad deal” — so the UK could be facing the ‘cliff edge’ of WTO rules at the two year point if a deal is not reached (or an extension agreed).

Like all things Brexit, sequencing of negotiations will not be simple — the future UK-EU trade relationship may impact on WTO terms (depending on the type of customs arrangement sought, the UK may need to keep the same WTO schedules as the EU), which in turn, will set the bar for FTAs to be negotiated with third countries. Defining what falls into the ‘divorce’ and the ‘remarriage’ will be a priority for both the UK and the EU, as it will also influence whether these negotiations should occur in parallel. WTO terms will govern the UK’s relationship with the rest of the world post-Brexit, so it is important to set these as soon as possible — to be implemented as soon as the UK exits the EU. The ‘remarriage’ of the UK-EU trade relationship will likely need to be agreed before any third country discussions can get very far — and similar to the WTO, it is only once the UK formally leaves the EU can it officially conclude these FTAs with third countries.

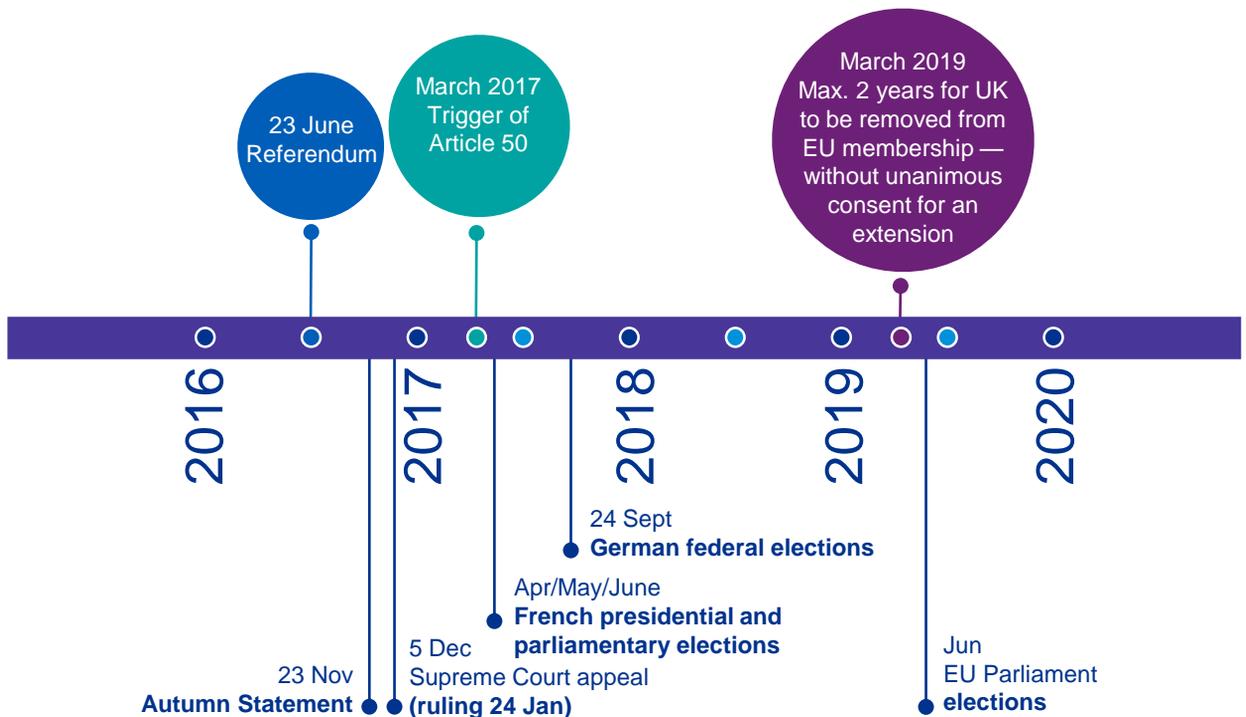
When will Brexit happen?

Until recently, the ‘when’ of the Article 50 notification rested in the hands of the Supreme Court. On 24 January 2017, the Court determined that the formal notification of UK’s departure requires an Act of Parliament — meaning both Houses of Parliament had to agree.

The UK Prime Minister was able to pass the Bill with no amendments, to trigger Article 50 in March as planned. The UK now has a maximum two year timeframe to agree the terms of the withdrawal (‘divorce’) — and ideally the future arrangement for the UK/EU relationship.

But in practice it isn’t really two years — the ‘exit’ deal will need to be agreed by the Council of the EU and the EU Parliament, while any future arrangement will likely require unanimity and national ratification by the remaining EU member states. May has also promised UK Parliament a vote, so the future arrangement would need to be determined in around 18 months to allow enough time to nut out the legalese.

The deal may provide for a transitional arrangement, to allow both UK and EU business to adjust to the ‘new normal’.



Source: KPMG’s Global Brexit Centre of Excellence

Italian elections?

What else should you be following...

The trigger of Article 50 will not only take place while the EU is distracted by the rise of the populist agenda in a number of national elections (Netherlands, France and Germany, with potential for Italy to follow suit), but also could be distracted at the other end — with election of the EU Parliament due to take place in June 2019.

And don't forget to keep an eye on the final ruling on the EUSFTA (Singapore-EU FTA) that will also be handed down. Late last year, the Advocate-General stated in a non-binding opinion that the Singapore-EU FTA will require ratification by all member states. It seems increasingly likely that any comprehensive agreement governing the future relationship between the EU and the UK will require unanimous approval of EU member states.

“Top Risks for 2017

#3 — A Weaker Merkel

Strong leadership from Angela Merkel has proven indispensable for Europe's ability to manage crisis in recent years. Europe will face more challenges in 2017— from France's elections, Greece's finances, Brexit negotiations, and delicate relations with both Russia and Turkey. Unfortunately, though Merkel is likely to win reelection as Germany's chancellor in 2017, she'll emerge as a weakened figure. This will leave Europe with no strong leadership at all — at a time when strong leaders are badly needed.”



What should you be thinking about now?

When there are so many moving parts, it is hard to know if you are keeping on top of things. Here's our recommended 'Survival Guide' for the next 12–18 months:

- **Decide upfront and clearly whether you want to be an influencer or a taker of outcomes:**
At every stage, you have the opportunity to have your voice heard in Westminster and/or Brussels — either on your own or through a business association or industry body. But engagement involves time, effort, cost and risk and you might decide that it's not worth it — but let that be an active choice with eyes wide open.
- **If you aren't already a scenario planner, become one:**
Optionality will be your greatest strength in this environment, but you can't have that unless you have imagined and planned for multiple outcomes. This does not need to be fancy — it just needs informed thought and credible challenge, both internally and externally.
- **Commit to a source of News, Intelligence & Analysis, and stick to it:**
You need to stay on top of developments, but it can be hard when so much is being said by so many different people. Pick a single, or at most two sources of news, intelligence and analysis and stick with them. It is better to pick the right source than to try and cover your bases from multiple sources, which can be paralyzing.
- **Think along the lines of known-knowns, known-unknowns & unknown-unknowns:**
It is a simple but helpful way to know what you can reasonably plan on the basis of. It would not be unreasonable to have a planning assumption that your migrant labor force declines by say, 25 percent. Or that the movement of goods will face border formalities, including tariffs, product/standard checks and rules of origin. Use these relative certainties to plan, and channel your remaining energy to tracking the known-unknowns and building resilience for the unknown-unknowns.
- **Never let a good crisis go to waste:**
Sure, the next 12–18 months will be turbulent but at the end of it, a new reality will be upon us and most businesses will come out the other side. Whether you come out stronger or weaker partially depends on what else you use this disruptive event to do. This may just be a convenient wrapper to do what's necessary and overdue; reorganizing the business, changing the operating model, investing in new markets, or simply raising the collective consciousness of the organization on geopolitical issues, of which Brexit is only one.

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