

Brexit Analysis Bulletin

House of Lords Committee Reports



The House of Lords European Union Committee has published six reports examining various aspects of the UK's current relationship with the EU, and the priorities it believes the Government should adopt in the Brexit negotiations. This bulletin highlights the key findings of the reports on Parliamentary Scrutiny, Financial Services and the UK's Options for Trade.

The reports come as part of a series of inquiries the House of Lords Committee is undertaking on EU-UK relations. Separately, the newly established 'House of Commons Exiting the European Union Committee' is undertaking its own enquiry on the UK's negotiating objectives for withdrawal from the EU; their first report was published on 14 January 2017 and the Government's response is awaited.

Parliamentary Scrutiny

This report examines the role of Parliament in scrutinising the Brexit negotiations. It considered evidence from various parties, including David Davis, the Secretary of State for Exiting the European Union. It comes in the context of an on-going constitutional debate about whether Parliament or the Government should have the final say in the negotiations, and was published just weeks before the Supreme Court ruled in the Brexit Case that Parliamentary approval was needed before ministers could trigger Article 50.

The report welcomes the Government's commitment to parliamentary oversight, and agrees that excessive scrutiny of Brexit could hamper the UK's freedom of manoeuvre during complex negotiations. Equally

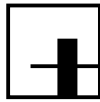
however, the Committee cautions against parliamentary scrutiny after the fact, given the enormous potential impact of Brexit on all aspects of UK life. It warns that refusing to offer a 'running commentary' could allow the resurrection of the "spirit of Sir Humphrey", the civil servant from comedy series *Yes Minister*.

The report concludes by calling for a middle ground between these two extremes, allowing Parliament to be consulted ahead of key decisions without hampering the Government negotiating strategy. It calls for parliamentary committees to be given access to negotiating documents ahead of time, and for the Government to be obliged to respond to Parliament's recommendations.

Since the report was published, the response from David Davis has been made available on the Committee's website. The Minister's response broadly welcomes the Committee's findings and commits to sharing information about the negotiations with Parliament as far as possible.

Financial Services

This report examines the impact of Brexit negotiations on the UK's financial services sector, which employs over a million people and contributes around 7 percent to GDP.



It notes that London is regarded as the world's leading financial centre, with a strong ecosystem of companies offering financial services; for example, London is the world's main centre for Euro-denominated clearing, despite being outside the Eurozone. The potential impact of Brexit on this sector is therefore significant.

The report makes a number of recommendations:

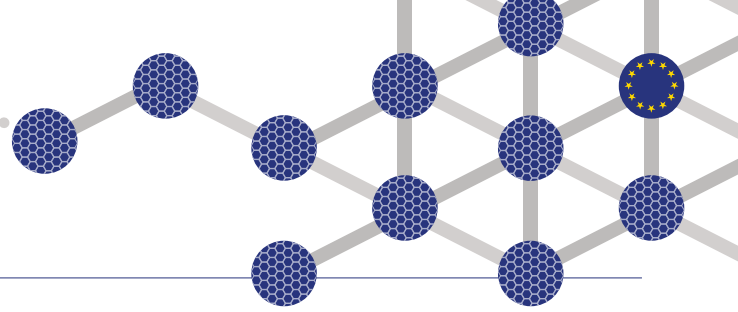
- The Government should urgently collect information on how, and how many, UK financial services companies rely on 'passporting' to sell their services into the EU. This process allows a financial services company based in one EU member state to trade in another without having to establish a subsidiary. As expert evidence to the Committee highlighted, many UK-based banks and other institutions rely on passporting to sell their services into the EU, but the legal regime that governs it is often misaligned with their internal structures. The Committee argues that without more information the Government cannot know what its passporting priorities should be.
- The Government should prepare for the potential loss of passporting by strengthening the current 'equivalence' regime. This allows countries outside the EU to trade within it by relying on their local regulations being 'equivalent' to those of the EU. As highlighted in evidence to the Committee, the current equivalence regime is patchy and underdeveloped in some areas, for example retail asset management.
- In light of the concerns about passporting and equivalence, the Government should place a high priority on agreeing a transitional period for financial regulations post-Brexit, as it will be extremely difficult to negotiate a final agreement within the two year period provided by Article 50. Without a transitional period, the Government risks the UK's status as a financial services hub, and companies taking steps – for example transferring staff to EU-based subsidiaries – on a 'worst case scenario' basis.

The Options for Trade

This report examines the various options available to the Government in respect of the UK's post-Brexit trading relationship with the EU. The UK is currently a member of the single market, which provides tariff-free trade within the EU and a customs union governing tariffs with external countries. Brexit will see the UK leave this arrangement, and a great deal of media coverage has focused on the post-Brexit trading options that the UK should pursue in the negotiations. Among the options considered are membership of the European Economic Area, a customs union with the EU, a free trade agreement, or trade on the basis of the World Trade Organisation (WTO) Rules.

The key tension, as highlighted by the report, is between a desire to ensure that UK companies have as few barriers as possible to trading within the EU, while also limiting the extent to which EU citizens are able to live and work in the UK without restriction. In this context, the key findings of the report are as follows:

- It argues that it will be very difficult for the UK to negotiate a version of any of these options that fully satisfies this tension. EEA membership is likely to entail free movement of EU citizens within the UK. A customs union would hamper the ability of the UK to negotiate trade deals with other parties (for instance the United States). A free trade agreement is unlikely to offer the level of tariff-free access that the UK currently enjoys. Trade on the basis of WTO rules is complex and depends on a series of bilateral negotiations which are yet to take place.
- Given the two-year timeframe provided by Article 50, the report argues the Government's priority should be a transitional agreement preserving current trading arrangements in some form, pending final agreement of the terms of what will replace it. This will avoid the 'cliff edge' of the UK's sudden exit from the single market and its replacement by underdeveloped WTO rules, and allow negotiations to take place in a less pressured environment.



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Now that the vote has been cast to leave the EU, members of our dedicated Brexit group continue to interrogate the regulatory and commercial issues and to advise clients on next steps and outcomes.

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