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Law Brexit brief

Brexit and long-term commercial contracts

It may be time to act now

More than 20 years has passed since the inception of the Single Market, originally proposed by the UK Government to its European Union (EU) colleagues. In that time trade between the UK and the EU has been stable and predictable and contracts entered into between UK entities and their EU counterparts have encouraged and facilitated trade, in part as contractual parties have been able to rely on the stability and predictability of their arrangements.



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The British referendum vote to leave the EU has introduced doubt as to the continued stability of trade between the EU and the UK, not least of all in the treatment of current and future trading arrangements. In this article we look at some of the issues facing trade between the UK and the EU after Brexit and some practical ideas of the steps that can be taken to safeguard against the dangers.

The vote to exit the EU has already caused significant market volatility and there will be continued uncertainty during the lengthy period in which post-exit arrangements are negotiated.

Cross-border trade between the UK and the rest of the world, whether with the rest of the EU (the EU takes almost half of the UK's exports and vice versa) or with third countries (the exit will leave UK business without the benefit of the 53 free trade deals which the EU has obtained) will be impacted significantly by Brexit.

The perceived benefits of the European Commission's digital single market project (being a set of policies designed to reduce on-line barriers to trade) for harmonization in areas such as platforms, geo-blocking, Audiovisual Media Services Directive reform and e-commerce and distant selling may not be forthcoming in relation to the UK. In particular, the UK will probably cease to be part of the customs union (import VAT may become due when goods enter the UK from the rest of EU and vice versa) resulting in volatility in tariffs.

There is a clear uncertainty as to the post-Brexit application of EU laws and regulations in the UK, and it is likely that, at least over time, we will see a patchwork of parallel EU, and UK-derived laws and regulations in place.

Although the UK Government will pass into UK law EU legislation already in force to ensure continuity, it is quite likely that it will seek to repeal certain aspects of EU-derived laws seen to be burdensome. It is also likely that the UK's implementation of new EU legislation may be delayed or suspended in the run-up to Brexit.

We expect the impact on commercial contracts to be high since these contracts are the backbone of trade across multiple sectors; in particular, retail and consumer products.

There is no reason to delay contingency planning and develop risk mitigation strategies, and it is better to act sooner to be best prepared. This is particularly true for commercial contracts, whether existing or planned contracts.

Change in law and regulation

It may be that, in practice, much of UK existing law and regulation will remain in place post-Brexit (amended to reflect the break with the EU), for example in the area of labelling (being CE marking, i.e. certification marking that indicates conformity with health, safety, and environmental protection standards), packaging and product standards, as UK businesses will still need to comply with these requirements to export products into the EU, irrespective of the equivalent national regulation. Other key UK legislation that is not derived from the EU, e.g. The Consumer Rights Act 2015, is not likely to change.

In some areas such as antitrust, there will probably be an additional layer of complexity, uncertainty and cost resulting from possible dual-regulation or parallel investigations post-Brexit.

The UK will look to construct a new legal environment and will flex its new found sovereignty on issues such as the choice of governing law of commercial contracts, international private law considerations, such as the recognition of the enforcement of foreign judgments in the UK, and any applicable foreign law. During this period, there will be significant uncertainty as to how existing contracts with a UK element are to be constructed, adjudicated and enforced.

Finally, businesses that manage to operate under a pan-European set of terms and conditions are likely to find that differences emerge after Brexit, and that UK law-specific terms are required for such terms and conditions to work effectively in the UK.

Practical consequences

Increased trade barriers: trade barriers between the UK and rest of the EU are likely to increase, meaning the cost of trade would increase.

Movement of people: freedom of EU nationals to travel to or reside in the UK and vice versa seems likely to be impacted by Brexit. This should be of particular importance in the service or retail industries where there is more frequent movement of people on a temporary or longer-term basis.

Currency fluctuations: the value of the pound versus euro may continue to fluctuate.

Territorial scope of contracts: the meaning of the EU territory is likely to change, depending on the nature of the EU's new relationship with the UK.

Parallel regulatory regime: parallel regulatory regimes under both UK and EU law are likely to emerge, dependent upon the nature of future relationships between the two partners.

Change in substantive law: although EU law that has been incorporated into UK law will not quickly fall away, the content of UK or EU law will progressively deviate, hence the need to use commercial clauses to mitigate the resulting uncertainty.

Governing law : the position of UK courts to determine the applicable law of a contract based on the EU Rome I Regulation in respect of contractual obligations is unlikely to change following Brexit, since UK common law principles are similar to those found in the Rome Regulation.

Enforcement of foreign judgments: if the enforcement mechanism under the Brussels Regulation ceases to be available then this could affect the way future judgments are enforced in EU Member States. Parties should consider taking advice as to how the enforcement of judgments will be dealt with in EU Member States where they have a presence or exposure if the Brussels Regulation ceases to apply between the UK and those Member States and the UK does not adopt a similar measure into its domestic law.

Outsourcing: the transfer of employees on the same terms where business activity transfers from one party to another (TUPE) is particularly relevant in outsourcing agreements. Following Brexit, even if the automatic principle is retained, there may be some relaxation of the terms on which it takes place and, consequently, the apportionment of costs in an outsourcing relationship may need to be revisited.

Agents: following Brexit, the UK may want to remove some protection for agents under the Commercial Agents (Council Directive) Regulations 1993 upon termination, thereby reducing the costs for principals. Conversely, agents may want to revisit their relationship with principals in order to incorporate these statutory protections contractually.

Recommended strategy for existing commercial contracts

It is prudent to audit existing contracts that have a connection with the UK and the rest of the EU and begin to assess the possible effects that Brexit may have on rights and obligations resulting from these contracts, including enforcement considerations and the right to terminate or the risks of being terminated, because of Brexit. Certain key items are listed below.

Increased trade barriers: assess the commercial impact of this increase on your contracts and, in light of this increase in costs, negotiate your position under your contracts.

Movement of people: assess whether the performance of the contract requires any movement of personnel from the UK to the rest of EU and vice versa, in which case, contingency planning may be required.

Currency fluctuations: assess the impact of the fluctuation of the pound versus euros, and whether said fluctuation could consist in an early termination/mandatory renegotiation event based on classical legal concepts such as hardship, frustration, material adverse change or force majeure etc.

Territorial scope: assess whether the definition of territorial scope of the contracts needs to be amended to reflect the possible exit of the UK from the EU.

Parallel regulatory regime: assess whether it is necessary to start negotiation on who will be responsible for achieving compliance and for noncompliance upon existence of a new applicable parallel regulatory regime.

Change in law: assess whether it is necessary to clarify the definition of applicable law to your contract. Are there reference to legislation as at the date the contracts is signed or does it incorporate "as amended" legislation? Remember that alterations of legislation following Brexit may have significant and unexpected effects on the parties' rights and obligations.

Early termination: assess whether Brexit may provide ground for early termination (by either party) under applicable law based on all particular terms and facts. Various legal concept could come into play: hardship, force majeure, frustration and material adverse changes. Analyze those further if you may have an interest in obtaining an early termination or on the other side, eliminating the risk that the other party would seek to obtain it.

Recommended strategy for new commercial contracts

When negotiating new contracts with a UK/EU 27 connection:

Increased trade barriers: you may wish to consider the extent to which prices should include or exclude any new taxes, duties or similar levies that the UK or EU Member States may introduce after Brexit takes effect.

Movement of persons: assess whether and to what extent you may circumvent the need to have personnel moving from the UK to the rest of the EU or vice versa for the performance of the contract (e.g., local subcontracting).

Currency/tariffs fluctuation: consider the more appropriate currency for the contract. Assess how to allocate the risk of future changes in the pound versus the euro; consider the potential impact of import tariffs and VAT changes. Consider including a price adjustment mechanism that covers potential additional costs arising from Brexit.

Territorial scope: define precisely the territorial scope of the contract to factor in the exit of the UK from the EU.

Parallel regulatory regime: negotiate who will be responsible for achieving compliance and for noncompliance upon existence of a new applicable parallel regulatory regime. Consider whether the performance of rights and obligations rely on EU competition/block exemptions.

Change in law: be mindful of the contractual impact of a change in law arising from Brexit over time and negotiate appropriate definitions in your new contracts. Remember that alterations of legislation following Brexit may have significant and unexpected effects on the parties' rights and obligations.

Early termination/renegotiation: be mindful to include or exclude Brexit as a cause for early termination or renegotiation of the contract in order to anticipate the possible effect of Brexit on the commercial viability of new commercial contracts, e.g., force majeure, material adverse change, hardship or frustration.

Duration: envisage converting long-term renewable contracts to short-term contracts to maintain the flexibility to negotiate new commercial terms over time. Consider this in light of the evolving Brexit timetable. Where relevant, use the timetable as a trigger for renegotiation or expiration of contracts.

Structure: consider whether the structure being put in place for the transaction may lead to future problems, e.g. withholding tax.

Dispute resolution: think carefully about dispute resolution clauses; these clauses should be drafted to make clear that courts are to have jurisdiction in the event of a dispute. Rules which address these issues are currently contained in the Brussels Regulation (which addresses issues of jurisdiction and enforcement). Arbitration will not be affected by the vote to leave, and consideration should therefore also be given to whether arbitration would be a better method of dispute resolution.

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