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## Brexit, Export Controls, Preferential Trade and Sanctions Programmes – Strategies and Tactics for Success Post-Brexit

**An Historic Referendum** On June 23, 2016, in an historic referendum, the United Kingdom voted to exit the European Union. In the aftermath of the referendum result, many companies are left wondering about the impact on their businesses as a result of potential changes to the export control, preferential trade, and sanctions programmes of both the United Kingdom and the European Union as a whole.

**Our Aim** We aim to help our clients approach the Brexit process in a goal-directed, structured and precise way against a background of unprecedented uncertainty requiring a measure of flexibility.

Our assumption is that our readers share a common goal—the desire to continue generating profit from their existing business relationships, although achieving that goal might involve doing things differently.<sup>1</sup> This will involve creating structures which continuously feed information updates to decision-makers to ensure that tactical decisions are made in a nimble, timely and precise fashion.

**The Problem Posed** In the context of export controls, preferential trade, and sanctions programs, the United Kingdom and the European Union have been (and for now continue to be) part of the same complex organism, the component parts of which dealt with each other by defined rules and faced the non-European Union world *broadly speaking* as one, applying the same rules. Conversely, the non-European Union world had become comfortable with the certainty of dealing with the European Union (for practical purposes) as one entity.<sup>2</sup>

Those complex and defined relationships are now destined to unravel and, in their unravelling, will cause commercial (and legal) anxiety for the following entities, all of which must now face the fluid nature of the new reality:

- Companies with a United Kingdom presence, United Kingdom-owned or otherwise, which have dealings with the Member States of the European Union (including selling to the European Union or relying on European Union suppliers) or the rest of the world through a European Union trade deal.
- Companies within the European Union that rely on United Kingdom suppliers, or for which the United Kingdom is an important export market.
- Companies, wherever based, which currently deal with the United Kingdom as part of the European Union, or as a gateway to the European Union Single Market.

**Recommendations** We recommend the following.

- To state the obvious, it is vital to create and thereafter to maintain a system of intelligence collection and analysis. There will doubtless be periods of lull, but information sources should be identified now and their contents monitored and collected daily (where appropriate) by someone capable of recognising relevance and importance. We expect that subscription news services will provide daily information. There are United Kingdom government-run websites, which will be the source of useful information. Depending on the developing attitude of the European Union, the European Union websites might contain useful information.
- In the context of the likely changes to sanctions regimes, identify whether your business collides with very politically sensitive regimes, such as the ones in respect of Russia or Syria.
- Take an inventory of existing export licenses and agreements that may be impacted by Brexit. This includes any U.S. export authorizations or exceptions that permit items or technology to flow between European Union Member States and/or nationals of European Union Member States. It also includes European Union General Export Authorizations that permit transfers of dual-use items and technologies to places outside the European Union. In certain instances, licenses/agreements may need eventually to be redrafted and/or applications made in the United Kingdom for new individual or general licenses in substitution for any European Union authorizations that fall away.
- Determine whether new export authorizations will be needed for trade of dual-use items between the United Kingdom and the European Union. It is particularly important for companies that rely on manufacturing in one jurisdiction or the other to factor in potential delays to their existing supply chain.
- Understand what duties/tariffs currently apply to your imports and exports as a result of the European Union's preferential trade agreements. Although we do not yet know what the United Kingdom will eventually negotiate with its trading partners, understanding where duties may be imposed will put

you ahead of your competition if you need to make adjustments to your supply chain.

- Determine what options are available if your company is relying exclusively on the United Kingdom as an access point into the European Union Single Market.
- If you are a United Kingdom manufacturer of goods subject to significant tariffs for those not part of the European Union, consider whether you should open operations in a European Union Member State.

**The Difficulties of Uncertainty** In summary, while we do not really know what will happen or precisely when it will start happening, companies need to begin preparing now for the inevitable changes, and remain flexible.

*The Timing of Notice under Article 50 of the Treaty of the European Union* It is impossible, at present, to be certain about when the United Kingdom will actually leave the European Union. The timing will depend on when Article 50 of the Treaty of the European Union is triggered, which provides<sup>3</sup> that “[a]ny Member State may decide to withdraw from the Union in accordance with its own constitutional requirements” and<sup>4</sup> “shall notify the European Council of its intention.”

Exit will occur within two years of that unless the European Council, in agreement with the Member State concerned, unanimously decides to extend this period, or will occur sooner in the event of an earlier-concluded withdrawal agreement.<sup>5</sup> The comments being made in the current febrile atmosphere do not suggest that any extension to the two-year period is likely. It is difficult to put it any higher than that.

It is tolerably clear that Article 50 (2) notice will not be given before the installation of a new Prime Minister and Cabinet. This is anticipated to occur after the Conservative Party Conference in October, but could well not be before the end of 2016. There appears to be uncertainty about the “constitutional requirements” involved in giving such notice, which may cause further uncertainty about the timing of the notice. In *The Times* of 30 June 2016, having said there were “powerful arguments on both sides”, Lord Pannick QC had expressed the view that an Act of Parliament was needed before the United Kingdom could give a notice under Article 50. Other leading QCs have expressed different views in the electronic letter comments of daily newspapers, supported most recently in a letter published in *The Times* of 4 July 2016, written by Lord Millet, a retired Law Lord.

It has now emerged that a legal challenge to clarify these “constitutional requirements” is being considered. As reported in both *The Times* and *The Guardian* of 4 July 2016, an anonymous group of clients have sought assurances from government lawyers over the process, and have retained the services of prominent constitutional law barristers Lord Pannick QC and Rhodri Thompson QC.

***The Substance of the Change*** Unless the European Union resiles from its avowed determination not to start even rudimentary preliminary negotiations with the United Kingdom, none will have any advance indications of the likely trajectory of the changes to come. In such a vacuum, multiple scenario-generation will be very important. We do, however, attempt to suggest possible trajectories based on early indications, drawing inferences from such evidence as there is and attempting to identify common interests, which might play a part after tempers have cooled.

**Impact on Export Controls** The United Kingdom is currently a member of several international agreements, such as the Wassenaar Arrangement, the Missile Technology Control Regime, the Nuclear Suppliers Group, and the Australia Group, in its own right. The Wassenaar Arrangement, for example, is a voluntary multilateral export control regime in which 41 countries are a part. This arrangement puts forth the List of Dual-Use Goods and Technologies and Munitions List, for which participating states must implement regulations to prevent the unauthorized export or re-export of controlled items. Being a member of the Wassenaar Arrangement requires that member states adhere to certain non-proliferation policies and maintain fully effective export controls. The United Kingdom's membership in these agreements is not dependent on its membership of the European Union, which will result in no immediate changes to its export regime, particularly for military goods.

Following the United Kingdom's exit from the European Union, however, there will likely be changes to how the United Kingdom and the European Union transfer dual-use items between their respective regimes. Currently, dual-use items may not leave European Union territory without an individual or general export authorization, but there is a general export license permitting the transfer of these items between European Union nations. While the United Kingdom is likely to continue exporting dual-use items to trusted European Union Member States with little change, the United Kingdom – given concerns regarding the uniformity of export control enforcement in certain member states – may impose stricter controls over exports to those countries. Thus, when Brexit takes effect, depending on what is negotiated between the United Kingdom and the remaining European Union nations, companies may now need to obtain export authorization to send certain dual-use items between the European Union and the United Kingdom.

As for U.S. export controls applied to the United Kingdom, they will remain largely unaffected by the United Kingdom's exit from the European Union. For the most part, the United Kingdom and the individual European Union Member States are recognized and treated as separate sovereign nations by the United States, not as part of the greater European Union. Entities in these countries will still be required to ensure necessary authorizations are in place for re-exports of U.S.-origin items or technical data controlled by the Export Administration Regulations (EAR), for dual-use items; or the International Traffic in Arms Regulations (ITAR), for defense articles.

The close, longstanding relationship between the United States and the United Kingdom will continue and could strengthen as a result of Brexit. Already the two countries have signed the Defense Trade Cooperation Treaty, which provides the basis for an ITAR licensing exemption for certain exports to the United Kingdom. The exemption facilitates the movement of defense articles and defense services between the United States and the United Kingdom, and permits the United Kingdom government and certain approved private sector entities to receive U.S.-origin defense articles/ services without licensing. U.S.-origin defense articles destined for the United Kingdom are also eligible for expedited license processing, when a license is required.

Under the EAR, the United Kingdom will continue to be recognized in “Country Group A:5,” which is subject to some of the least restrictive export controls. Certain license exceptions such as Strategic Trade Authorization (STA), will continue to be available for certain exports, re-exports, and transfers that would otherwise require a license.

**Impact on Sanctions Programs** Nothing will change until the United Kingdom formally leaves the European Union. According to one report,<sup>6</sup> after Brexit, the House of Commons Foreign Affairs Committee has said that “government could adopt a ‘policy mirroring’ approach and continue to align itself to EU sanctions regimes – a method that is currently being employed by some non-EU Member States such as Switzerland and Norway – or increase its own autonomous sanctions powers and grant more authority to its national enforcement agencies, such as the Office of Financial Sanctions Implementation (‘OFSI’), launched earlier in the year.” We return to possible outcomes below.

There are currently three types of European Union sanctions:

- Those agreed at the United Nations Security Council (UNSC), which all Member States are required to adopt. After Brexit, the United Kingdom must and will continue to implement and enforce such sanctions by dint of its membership. These include Cote d’Ivoire and the Central African Republic.
- Those that supplement UNSC sanctions; the Iran and North Korea regimes are an example. In the case of Iran, Council Regulation (EU) No 267 of 2012 was amended to reflect the Joint Comprehensive Plan of Action (JCPOA), to which the United Kingdom is an individual subsidiary. That being so, at least initially post-Brexit, the United Kingdom will have to do what’s necessary to continue to give effect to its obligations under the JCPOA.
- Autonomous European Union sanctions that are put in place in the absence of UNSC sanctions, for example, in respect of Russia. Russia wielded its veto in the UNSC to block a resolution on Ukraine. Russia and China vetoed proposed resolutions for Syria. In this context, the outcome is less certain, a matter to which we return below.

There are, however, uncertainties derived from future potential divergence between European Union and United Kingdom approaches in this area.

The current European Union sanctions regimes reflect a particular decision-making dynamic. As EU sanctions programmes require unanimity and apply to all EU members, Member States were prepared to accept the economic pain involved in imposing sanctions on third-party countries because the pain was shared, and no individual Member State needed to be concerned that any other Member State could gain an advantage by adopting a different policy. It was, as it were, all for one and one for all.

The European Union Russia/Ukraine sanctions regimes provide a powerful example. The consensus appears to be that the United Kingdom was and is a strong proponent of these regimes and continues to champion their renewal. The pain caused by these regimes has been felt to different degrees in individual Member States. It may be that, absent United Kingdom involvement, the European Union decision-making dynamic might change and the current regime either be allowed to lapse or, alternatively, be liberalised. In either event, the European Union would gain an economic advantage over the United Kingdom by having resumed fuller trading relations with Russia.

Faced with such competition from its former partners, the United Kingdom government would then have to decide whether it was either possible or desirable to continue a hardline approach to Russia. If, on the other hand, the United Kingdom government did decide to pass legislation to maintain that approach, or possibly aligned itself even further with the United States, the resulting divergence could create regulatory issues for institutions with operations both in the European Union and the United Kingdom.

**Preferential Trade Programs** The United Kingdom's participation in various free trade agreements will be impacted on its exit from the European Union, as the United Kingdom will no longer be a party to the approximately 58 EU-negotiated trade agreements and their preferential programs.

Because the United Kingdom will have to negotiate and implement separate trade agreements, the extent to which Brexit will impact tariffs – and thus the cost of doing business – is also unknown at this point. Companies may face significant tariff changes in light of Brexit. Alternatives the United Kingdom may consider are joining the European Economic Area (like Norway), negotiating bilateral deals with the European Union, or dealing with the EU merely as a member of the World Trade Organization.

The indication from the European Union is that the United Kingdom will not be a full participant in the Single Market, unless the United Kingdom is prepared to accept the free movement of people. This is likely to be the major sticking point, as it is a sovereignty issue at the heart of the dispute.

If you have any queries about the contents of this alert or about sanctions regimes in general, please contact one of the authors of this alert, [sanctionsteam@reedsmith.com](mailto:sanctionsteam@reedsmith.com), or your usual contact at Reed Smith.

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- <sup>1</sup> We accept and recommend that prudent planning would and should also involve simultaneously identifying and analysing new and alternative business relationships. But that is not the focus of this document.
  - <sup>2</sup> We make a broad point in an organisation, which has a balance of competences.
  - <sup>3</sup> See Article 50 (1).
  - <sup>4</sup> See Article 50 (2).
  - <sup>5</sup> See Article 50 (3).
  - <sup>6</sup> See WorldECR, <https://www.worldecr.com/uk-to-re-assess-its-sanctions-regimes-after-brexit-vote/> accessed 30 June 2016.

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