

Brexit – Implications for Business between Swiss and UK Companies

24.06.2016

This Legal Update provides an overview of selected Brexit implications for the business between Swiss and UK companies from a Swiss law perspective. In particular, it addresses the questions whether existing Swiss law contracts are affected or need to be amended and whether new contracts should provide for special provisions addressing Brexit. It also highlights some tax aspects.

Key takeaways:

- The vote in favor of Brexit has no immediate legal effects on the legal framework between Switzerland and the UK and on Swiss law governed contracts
- Uncertainty and risks related to Brexit are to be considered in future M&A, JV and financing transactions
- Particular caution is recommended in connection with M&A and JV transactions in EU regulated sectors (e.g., banking, insurance)
- To ensure that dividend withholding tax relief at source remains available, companies should timely file a request under the double tax treaty UK / Switzerland

1. Overview

On Thursday, 23 June 2016, the UK has voted in favor of Brexit, the British exit from the EU. The vote in favor of Brexit should have no immediate legal effects on the legal framework between Switzerland and the UK and on Swiss law governed contracts (see Section 4). But in the coming months, UK and EU leaders will start negotiations on the terms of Britain's exit and the future reciprocal market access in respect of goods, persons, services and capital. The negotiations are expected to take several years and there is no saying, at this time, how and to what extent reciprocal market access will be granted.

In parallel, Switzerland and the UK are expected to agree on a new basis for the regulation of the trade between Switzerland and the UK which is currently governed by bilateral agreements

between the EU (including UK) and Switzerland.

Because, at this time, the scope of application of such an agreement between Switzerland and the UK cannot be predicted, there is no saying which aspects of business between Swiss and UK companies will be governed by such an agreement and which aspects will be governed by national laws (i.e., Swiss or UK law). There is an uncertainty as to which rules will apply and what their content will be.

In the following, we highlight some of the expected legal implications.

2. M&A-Transactions and JV-Partnerships

The vote in favor of Brexit should have no immediate legal effects on M&A-Transactions and JV-partnerships, unless such effects have been contractually agreed or in very exceptional cases (see also Section 4).

In view of Brexit itself, parties to future M&A transactions and JV-partnerships in which the target or JV-company is located in the UK, should consider (i) how the uncertainty on the applicable rules affects the transaction, the business or the legal situation of the target or the JV-company and (ii) to what extent this uncertainty or potential risks should be addressed in the transaction agreements.

For example, targets or JV-partners being:

- banks, insurers or other companies doing business in the UK currently benefiting from regulatory initiatives aimed at ensuring an integration of EU financial markets, may no longer benefit from the same advantages or may have to deal with uncertainties;
- and, vice versa, banks, insurers or other companies incorporated in a EU member state currently benefiting from regulatory initiatives aimed at ensuring an integration of EU financial markets, may no longer benefit from their access to the UK market and its financial centre;
- companies doing UK business which depends on existing EU Trade Marks (EUTMs) and Community Designs (CDs) may have to convert their EUTM or registered CD to or register for UK national trademarks and designs to preserve protection (and incur the costs in doing so); and, vice versa, there may be some uncertainty whether they can achieve to preserve their priority and existing EUTM registrations that have predominantly been used in the UK, are at risk of nullification for non-use in the EU, since their owners would not be able to demonstrate use in a substantial part of the EU.

3. Financing and Capital Market Transactions

The vote in favor of Brexit should have no immediate legal effects on debt and equity financings, unless such effects have been contractually agreed or in very exceptional cases (see also Section 4). Swiss standard terms for lending and bond transactions do not, however, provide for an event of default or an interest step up as a direct consequence of Brexit.

Brexit itself, however, may adversely affect the business of Swiss (or foreign) companies or groups, particularly those (i) having a substantial part of their business in the UK or are otherwise exposed to the uncertainties triggered by Brexit (see examples in Section 2) (ii) Swiss (or foreign) banks as borrowers to such companies, or (iii) Swiss (or foreign) group companies providing a guarantee or security to the benefit of a group company doing business in the UK and which obtains a financing.

In the context of a lending transaction, financial covenants would respond to a deterioration of a borrowers creditworthiness. In the context of a bond transaction such deterioration may cause a downgrade of the issuer leading to an interest rate step up.

In amendments or restructurings of existing financings as well as in future financings, borrowers, issuers, guarantors/obligors and involved banks should consider addressing the uncertainty and potential risks caused by Brexit. For example, bond issuers may consider inserting Brexit specific risk factors in the offering documents.

In addition, Swiss (or foreign) companies issuing bonds need to consider that currently the EU prospectus regime does not allow for the passporting of prospectuses to non EEA countries. Following Brexit, Swiss issuers who listed their bonds in Switzerland and obtained a secondary listing in the EU may need to have their prospectuses approved by the UK authority before offering securities in the UK.

4. Existing Contracts

The vote in favor of Brexit should have no immediate legal effects on Swiss law governed contracts concluded between Swiss or UK companies, unless such effects have been contractually agreed or in very exceptional cases.

As such, neither the vote in favor of Brexit, nor Brexit itself, are expected to cause nonenforceability or to trigger extraordinary termination rights. Statutory rights regarding termination, contract adaption for changed circumstances (*clausula rebus sic stantibus*), economic impossibility or material error will only trigger in very exceptional circumstances.

Nevertheless, a case-by-case analysis is recommended should particular negative consequences for a specific contract follow from Brexit.

5. Governing Law and Jurisdiction Clauses

Brexit may eventually lead to some changes in the conflict of law rules in England and to a new instrument addressing international jurisdiction and the recognition and the enforcement of English judgments in Switzerland and Swiss judgments in England.

Currently the UK has enacted the Rome I regulation on the law applicable to contractual obligations, which applies if jurisdiction is referred to English courts, irrespective of the fact that the counterparty is domiciled in a non-EU member state. Although there is some uncertainty as to the future, post-Brexit conflict of laws regime in the UK, it can be assumed that the UK will continue to recognize choice of law clauses in the b2b context.

At present, free movement of judgments between Switzerland and the UK (as part of the EU) is ensured by the Lugano Convention on Jurisdiction and the Recognition and Enforcement of Judgments in Civil and Commercial Matters. When the UK exits the EU, the UK could become a party to the Lugano Convention, considering that the Lugano Convention is open for accession to non-EU member states (but would require that either (i) the UK becomes an EFTA member or (ii) all existing member states of the Lugano Convention unanimously agree to the accession).

Although it seems unlikely that the UK will not be in a position to join the Lugano Convention or enter into a similar instrument, arguably the present situation leaves some uncertainty regarding the future enforcement procedure.

This uncertainty might foster the use of arbitration clauses, given that the enforceability of arbitral awards is ensured by the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards to which both the UK and Switzerland are member states. The Hague Convention on Choice of Court Agreements might also become a future alternative; at present, however, Switzerland is not a party to this Convention, and it is uncertain whether the UK will join it after it becomes independent of the EU (currently, the UK is a member by signature of the EU).

6. Dividend Withholding Tax

Dividends paid to or received from UK group companies are exempt from dividend withholding tax under the EU / Swiss Savings Agreement (WHT zero rate). The benefits of the EU / Swiss Savings Agreement should no longer be available once the UK has left the EU.

Relief from dividend withholding tax will then have to be sought - exclusively - under the double tax treaty UK / Switzerland. Alike the EU / Swiss Savings Agreement, the double tax treaty UK / Switzerland provides for a WHT zero rate (i.e. full withholding tax relief) for qualifying participations. However, the procedures are different. In particular, the Swiss advance permit to apply the notification procedure (withholding tax relief at source) under the double tax treaty UK / Switzerland must be applied for using a different form.

7. EU Financial Transaction Tax (EU FTT)

Swiss financial institutions, such as in particular, Swiss banks, are closely monitoring plans to introduce an EU FTT. The tax is likely to be introduced in a form such that it would be owed not only by financial institutions in the EU, but also by Swiss financial institutions performing an in-scope transaction. As an EU member, the UK strongly opposed the suggested EU FTT. With Brexit, the UK will lose its ability to participate in the EU decision taking. Thus, it can be expected that it will be easier for the countries in support of the EU FTT to move this legislative project forward.

8. Summary and Recommendations

The vote in favor of Brexit should have no immediate legal effects.

However, the uncertainty and potential risks related to the actual Brexit following in a few years, should be considered when entering into M&A, JV and financing transactions. This holds particularly true for transactions in the banking or insurance sector when the business relies on regulatory initiatives aimed at ensuring an integration of EU financial markets, because such businesses may no longer be able to benefit from such initiatives.

As the future legal framework is not yet predictable, specific Brexit provisions need careful drafting. For example, as of today, generic or detailed Brexit provisions in contracts and transaction agreements are at risk to limit future flexibility and may inadvertently override otherwise helpful (Swiss or foreign) legislation regulating Brexit.

With respect to tax, to ensure that dividend withholding tax relief at source remains available, it is recommended filing a request under the double tax treaty UK / Switzerland early enough to obtain a double tax treaty notification procedure permit from the Swiss tax authorities before the UK leaves the EU (i.e. replacement of existing permits under the EU / Swiss Savings Agreement).

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