

A Risk-Based Brexit Solution

As family enterprise risk managers we at Termes believe that the terms of trade post Brexit are the main focus around which business risks will have to be managed. Business owners and managers cannot afford to be passive bystanders or even, for that matter, partisan advocates about Brexit. Risk management measures made necessary for UK businesses by the British decision to exit the EU should not be concerned with who is right in the debate before and since the vote to leave was held.

Is Trade Important?

Why does trade matter? Trading takes place between two countries because both benefit by creating products where each has a comparative advantage and exchanging them rather than each country trying to produce everything itself. The fact that billions of pounds-worth of international trade takes place all around the world seems to provide conclusive evidence in support of this assertion. So yes, trade does matter, because in general it produces economic benefits and improves people's lives.

Do trade agreements matter? Yes – the UK mainly exports relatively sophisticated products and services, and another country will unlikely permit UK exports to enter its borders if they do not meet minimum product quality and testing standards; or, if they were produced by infringing the intellectual property rights of one of its citizens or corporations. And the best way to ensure these requirements are met is to reach agreement at a governmental level over what they should look like.

If trade matters, and it is facilitated by trade agreements, why would the UK abandon the vast amount of work that has gone into facilitating trade with the EU in favour of starting again at the WTO level? This is not a sensible option – indeed, one might say it is plain irrational.

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It's Not Just About Trade – Politics is Key

So, what is the best mechanism to achieve Brexit whilst facilitating UK-EU trade? Well, it is crucial to recognise that Brexit is not just about trade. There are political aspirations as well. These include: the desire to leave the EU; to place a limit on immigration from the EU; to remove the UK from the jurisdiction of the European Court of Justice; to create its own trade deals with non-EU countries and to avoid a breakup of the UK. However, there are also aspirations to minimise adverse effects on UK-EU cooperation in terms not just of trade, but also national security, immigration from non-EU countries, science and education.

And what is on the wish-list of the EU regarding Brexit? The desire to preserve the principles upon which the single market was founded – that full access depends on participants agreeing to the free movement of goods, services, capital and people across national boundaries. EU members also wish to discourage secessionist tendencies (which are on the rise) amongst its members, by demonstrating that Brexit will involve substantial “cost” to the UK. But they also share with the UK the desire to minimise adverse effects on UK-EU cooperation in terms of trade, security, immigration from non-EU countries, science and education.

Finding a Solution by Dealing with Uncertainty

Where are we so far? We have established the importance of continued high levels of UK-EU cooperation and trade, but identified many factors that seem to force the two sides apart. How can these tensions best be resolved? We argue the only way to do this is by minimising uncertainty. Why is this? Uncertainty is always bad, because policy-making and economic activity require the ability to make rational decisions in a complex world. More uncertainty leads to less decision-making and therefore political deadlock and less economic activity.

There are two dimensions to Brexit strategy uncertainty – the viability of the strategy (i.e. the degree to which it preserves the aims of both sides), and the time the strategy can reasonably be expected to take to implement (the longer the time, the greater the uncertainty).

When two parties come together with the basic desire to reach an agreement over something, but subject to the achievement of often conflicting aims, they look for precedents. They ask the question: “How have such agreements been achieved in the past, under similar circumstances?” Identifying precedents as the basis for an agreement represents a quantum leap towards minimizing both dimensions of uncertainty – they provide information about the detailed workings of a solution that support viability, and help to clarify where modification is required to suit each party’s actual aims, thereby helping identify a realistic timeline and road map for negotiations.

The Solution in Detail

We believe that Brexit can best be achieved by negotiating a comprehensive Association Agreement, which would define the UK’s entire relationship with the EU, including a free trade agreement, and incentivising UK companies to employ more domestic workers through a package of tax incentives.

The recently negotiated Association Agreement between the EU and the Ukraine serves as a possible precedent for Brexit and facilitates exit of the UK from the EU whilst permitting free movement of goods, services and capital between the two. Existing EU directives (which are implemented by national legislation and already part of UK law) would remain unchanged. Existing EU regulations (which are directly applicable to EU members without further supporting national legislation) will be repealed but mostly (because they are mainly product-specific technical standards) “cut and pasted” into UK law during the 2 year post-Article 50 period. The UK would develop a legal mechanism to define new UK laws and standards, both independently and in response to new EU directives and regulations, to balance the requirements for legal sovereignty with the need to retain access to the EU market.

The Association Agreement will cover every aspect of the UK’s relationship with the EU by setting out all of the relevant EU directives and regulations which apply, in the following key areas:

- Trade and trade-related matters, through the implementation of a “Deep and Comprehensive Free Trade Agreement” (DCFTA);
- Economic and sector cooperation;
- Financial cooperation, and
- Institutional provisions

A more detailed commentary on these provisions is contained in the PDF version of this blog which can be downloaded by clicking on the link.

An immigration proposal that builds on the precedent set by agreement reached between the EU and Switzerland late last year is also realistic. Employers in certain areas of activity, professional groups and economic regions will have to notify vacancies to unemployment offices if unemployment is above average in these groups. These vacancies are available exclusively to the jobseekers that are registered at the unemployment offices for a certain period of time and the unemployment agency must provide the employer with details of potentially suitable candidates. Employers must consider these details and invite candidates to interviews.

We propose going beyond the Swiss model by including incentives which would enable employers to offset the cost of training, travel and accommodation against tax. So for example, a construction firm seeking 200 new staff for a 2 year project in Hertfordshire would be able to encourage workers from a relatively high unemployment area like the North-East of England by offering them a pay and compensation package including on-the-job training, the cost of rented accommodation, and weekly travel to and from home. The cost of this package would be claimed by the company against its taxable income.

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