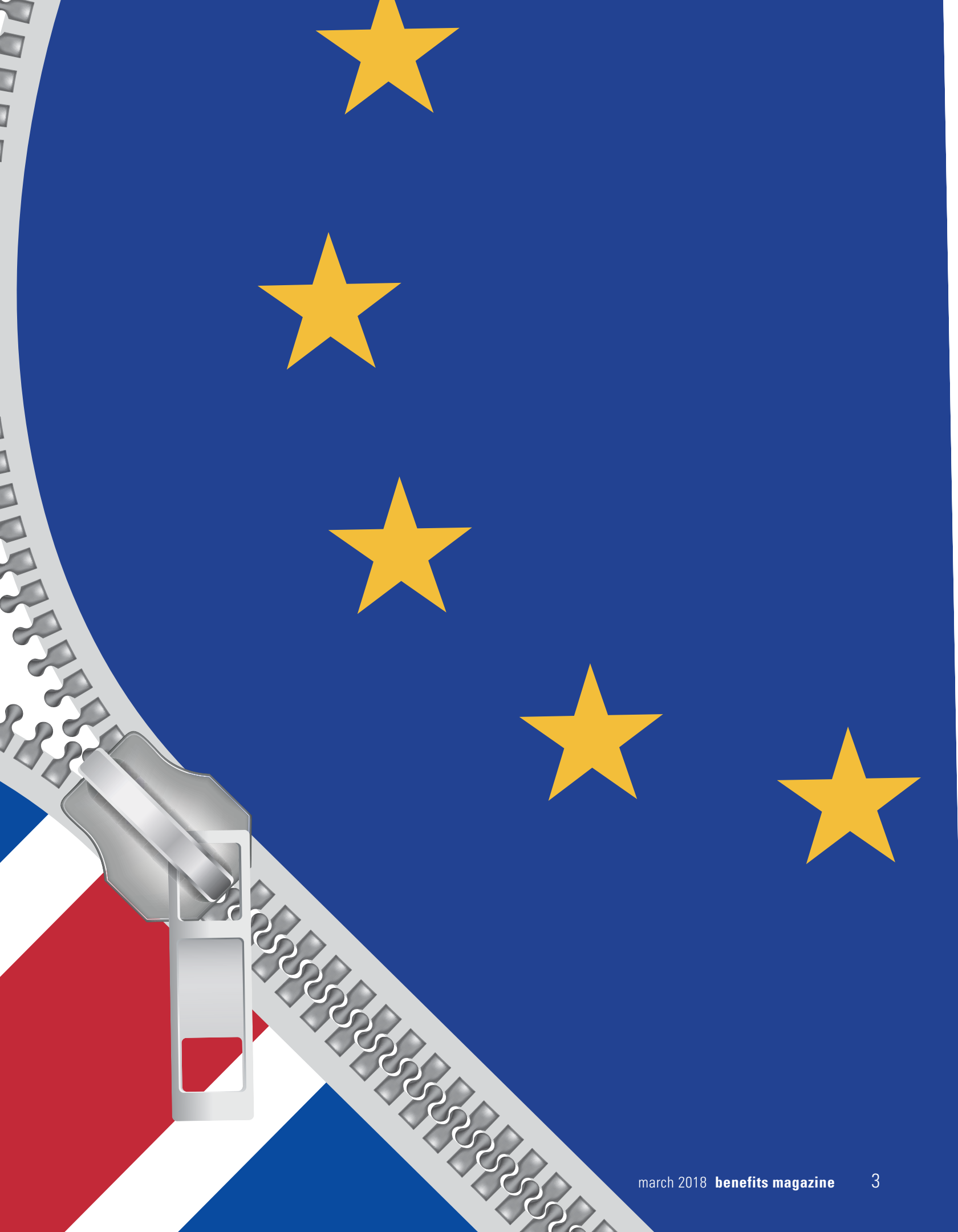


U.S. multinational companies are assessing the impact of Brexit on their European businesses, regional talent strategy and employee benefit plans.

# How Are U.S. Multinationals Preparing for Brexit?

by | **Selima Crum** and  
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Since the June 2016 referendum in which British citizens voted to exit the European Union (EU), significant uncertainty about the United Kingdom's future relations with the EU has made it largely impossible for multinational companies to plan for the impact that Brexit may have on their European businesses, regional talent strategy and associated employee benefit plans. No one doubts that there will be consequences, but the nature and severity of those consequences are tied to still nebulous possibilities, like whether there will be a "hard" or "soft" exit and whether new trade negotiations critical to ensuring the continued free flow of goods, services and people can even begin prior to the remaining 27 member nations approving terms of the separation, which is formally scheduled for March 2019.

Yet Britain's unprecedented exit is not the only recent threat to EU stability that has required careful risk assessment by global human resources professionals. Over the past ten years, the EU's single-market ambitions—of central interest to multinational companies—have been threatened by a major financial crisis, the Greek debt crisis, Russian aggression in the Ukraine, politically contentious immigration flows, high unemployment in many nations and an escalating number of terrorist attacks. All of these challenges add to the growing uncertainty about Europe's ability to deepen its union, making it increasingly important for companies to evaluate the possibility of increased fragmentation and complexity.

The U.K. has long been one of the first countries into which U.S. multinationals are most likely to expand. Much

of Britain's attractiveness to U.S. business will remain unaffected by Brexit: a common language, longstanding historical and cultural ties, and the relative ease of setting up and doing business. But other equally important factors that have made the U.K. such an obvious place to locate a European hub are threatened. London may prove unable to defend its position as the financial heart of Europe, and important privileges granted with EU membership—particularly the ability to transact business across borders under financial "passporting" and freedom-of-services provisions—may end.

Most U.S. companies appear to be taking a wait-and-see approach because there are too many unknowns. However, many have begun evaluating their options, and a growing number are already making preemptive strategic decisions about where to relocate specific business activities and how to best insulate themselves from a worst-case scenario.

The potential end of direct and unfettered access to EU markets has pushed financial services companies to consider alternative hubs for their European business activities. HSBC, Citigroup, Goldman Sachs, JPMorgan, Morgan Stanley and Nomura are among the banks and investment firms that have announced staff relocation plans. Even Lloyd's of London is opening a subsidiary in Brussels. Legal and professional services firms that work with the financial industry are following their clients. Pharmaceutical and high-tech companies have been particularly concerned about their future ability to attract and retain quality foreign talent in the U.K. More than a quarter of the academic staff of U.K. universities are non-U.K. nationals, and among those working in science, technology, engineering and math approximately 17% are EU nationals. Some 25% of the pharmaceutical industry's 73,000 employees come from abroad.<sup>1</sup> Conversely, and equally troubling, 63% of EU companies surveyed in October 2017 by the Chartered Institute of Procurement & Supply (CIPS) said they planned to move some of their supply chain out of the U.K., up from only 44% in May 2017.<sup>2</sup>

All businesses in the U.K. will face challenges as the government evaluates how to replace broad areas of employment law that were directly and indirectly dependent on the EU, particularly in the areas of the right to work across borders and the reciprocity of social insurance protections.

## Where Things Stand With Brexit

From its origins in the European Coal and Steel Community (Treaty of Paris, 1951), the overarching ambition of the

## takeaways

- Following a June 2016 referendum, the United Kingdom is scheduled to exit the European Union (EU) in 2019.
- The U.K. has long been one of the first countries into which U.S. multinationals are most likely to expand and will remain attractive, but many multinationals are considering an alternative hub for European business activities.
- One important area that may be affected includes the ability to transact business across borders under financial "passporting" and freedom-of-services provisions.
- Some areas of employment law that were dependent on the EU, including the right to work across borders and the reciprocity of social insurance protection, also may need to be replaced.

EU has been to establish a single European market for goods, services, and labor—a union that would make another world war materially impossible. The union has faced many challenges, but the British referendum constitutes its most profound existential threat. Previously unthinkable, the possibility of dissolution is now officially open for debate. After the British vote, EU member states launched a “political reflection process,” during which EU leaders discussed possible reforms to tackle new security and economic issues threatening the EU, as well as next steps following the British referendum.<sup>3</sup>

The U.K. will have to comply with EU legislation until the withdrawal agreement is finalized.<sup>4</sup> The agreement will address legal, financial and strategic issues, such as the financial settlement to be paid to the EU, freedom of movement, EU insurance and pension plans, as well as future compliance with EU legislation. Preliminary agreement has been reached on settlement payments, and the European Commission announced in December 2017 that it was open to a transition period through December 31, 2020. During that time, the U.K. would be required to follow all EU legislation and judgments, but it would not have a voice in any EU institutions after March 30, 2019.<sup>5</sup>

### Freedom to Provide Services

The single market for services is a core EU principle that grants the freedom to provide or receive services in a European Economic Area (EEA) country other than the one where the company or consumer is established. When the U.K. leaves the EU, there may be significant consequences for companies relying on their U.K. location and its li-

censes to transact cross-border business (known as *passport privileges*) within the EU customs union and single market. The U.K. government has repeatedly stated that it will reach an agreement permitting U.K. businesses to continue unfettered trading activities, but negotiations have not yet begun.<sup>6</sup> The U.K. will have to choose a new or an existing free-trade deal with the EU, modeled on the World Trade Organization (WTO) or the Norwegian, Swiss, Turkish or Canadian trade deals.<sup>7</sup> Transitional provisions may be negotiated with the EU before Brexit to ensure a smooth transition, but one of the primary drivers behind Britain’s “leave” vote was the desire to end another EU core principle—freedom of movement—which the EU will use as its primary bargaining chip in future trade negotiations.

At present, U.K.-based financial institutions will no longer have passporting rights<sup>8</sup> and, therefore, wouldn’t be able to sell financial services into the EU market. Multinational and U.S. corporations may need to open offices within an EU member state to be able to sell services into the EU market. However, the U.K. government contends that an “equivalent”<sup>9</sup> to the EU passport will be established. It is still unclear how this equivalent would allow financial institutions to continue to sell their services in Europe and if the U.K. will be able to join the EEA to keep the passporting rights.<sup>10</sup> Further negotiations between the U.K. and the EU would clarify the nature of this arrangement, which is crucial for the U.K. economy since around 5,500 financial institutions rely on the passporting rights in the U.K.<sup>11</sup> The impact of Brexit is already being felt in London’s financial services industry, which has experienced the biggest decline in

available jobs since the referendum as in the preceding five years, according to recruiter Morgan McKinley.<sup>12</sup>

Of specific relevance to employee benefits is the impact on U.K. domestic and cross-border insurance services that have flourished under EU freedom-of-services provisions. For years, global insurers and financial institutions have sought to leverage London markets and expand their business by taking greater advantage of the ability to write insurance contracts in one European jurisdiction that cover risk in another. This has been integral to Lloyd’s European business strategy and also to other EEA insurers that rely on their U.K. branch passport to access the London market. U.K. insurers that currently use their passporting rights in the EEA member states may need to relocate in an EEA state in order to continue providing services within the region.<sup>13</sup>

Multinationals also have benefited from insurance freedom-of-services provisions by using a U.K.-written policy, whether life, disability, personal accident or travel accident, to cover the employees and risks of their other European businesses. Conversely, they have sought coverage in the London market that wasn’t readily available in their local EU national market. These facilities may no longer be possible and, while it will not be difficult to decouple such cross-border arrangements, it will likely add to cost and complexity. Further, it represents an undesirable regression from progress previously made in simplifying and unifying European employee benefits arrangements.

### Freedom of Movement

Among the three primary topics addressed in the first phase of nego-

tiation between the U.K. and the EU is one of critical importance to multinationals—EU nationals' rights to free movement and the immigration status of the approximately one million U.K. nationals working in the EU. The two parties have tentatively agreed to maintain free movement, without a visa, for workers, students, family members and self-sufficient EU citizens living in the U.K. at the time of separation. Those individuals would be considered legally resident, and declaratory residence documents would be issued for them at no cost or at a minimum cost once the withdrawal agreement enters into force.<sup>14</sup> According to the U.K. Office of National Statistics, EU nationals comprise approximately 7% (2.3 million) of the current U.K. labor force, with the highest proportional representation in the wholesale and retail trade, the hotels and restaurants sector, followed by financial and business services. However, unemployed EU citizens living in the U.K. may not be able to receive social assistance benefits.<sup>15</sup> Job seekers would not be allowed to reside in the U.K. unless they secure a job offer, and quotas for low-skilled workers would be introduced. Also, the U.K. will be able to restrict the free movement of EU citizens when they represent a threat to public security, public health or public policy.

It is still unclear how this flexible immigration policy would work in the future and if it will remain under future governments. Free movement between the EU and the U.K. will end on March 29, 2019, and the rights of EU citizens residing in the U.K. at that time will be enforced by the British courts without any obligation to seek the opinion of or right of appeal to the European Court

of Justice.<sup>16</sup> These new restrictions are likely to increase compliance costs and make it more difficult to attract highly skilled workers in the U.K. Long a uniquely attractive country for highly skilled and ambitious global talent, the U.K. has already become less attractive to EU and other foreign nationals seeking career opportunities and a place to build a future.<sup>17</sup> Post-Brexit, the U.K. government will determine its own immigration policies, which may present new immigration paradigms for EU citizens, as well as nationals from other parts of the world, including the United States. Despite the many uncertainties, U.K. employers should begin informing their EU citizen employees how they can secure continued residency and the right to work in the U.K. Public guidance is available on the government's Brexit website ([www.gov.uk/world/brexit](http://www.gov.uk/world/brexit)), but companies will likely wish to seek advice and assistance from their immigration counsel.

## EU Social Health Insurance

### *European Health Insurance Card*

The European Health Insurance Card (EHIC) provides U.K. travelers with access to free health care or reduced price health care in the EU and the EEA states. An estimated 27 million U.K. citizens have EHIC. The British government promised to negotiate a new arrangement similar to the existing EHIC to facilitate travel between the U.K. and the EU.<sup>18</sup> Until an equivalent is negotiated or the U.K. decides to join the EEA, U.K. nationals traveling in Europe won't be treated the same as the residents of European member states since they will lose their EHIC benefits. Many U.K. employers, even those that are multinational

subsidiaries, do not cover their business travelers for urgent care medical expenses, particularly if their business travel is largely restricted to the EU. Those businesses will need to provide this coverage for business travel and even give employees the option to extend it to personal leisure travel because they may no longer be able to rely on their EHIC coverage.

### *Reciprocal Health Care*

EU citizens can currently move to any member state and get the same health care services as local national citizens as well as take their social security, pension and health care entitlements with them. U.K. nationals living in a European member state could lose their reciprocal health care rights, which would force them to pay much more for private health care. U.K. citizens living in other member states are covered by the host country national health service. The U.K. will have to reach a deal with the EU to ensure that its retirees living abroad, mainly in Spain (which has more than 200,000 retirees) and also in Ireland, Italy, Cyprus and France, don't lose their rights and be forced to return to the U.K.<sup>19</sup> Employers may see greater employee demand for private medical insurance and the ability to extend coverage internationally. Unlike most U.S. health insurance, neither U.K. national health nor standard private medical insurance covers medical expenses incurred outside of the country.

## EU Pension Schemes

### *The IORP II Pensions Directive*

After two years of negotiations, the updated EU directive on occupational retirement plans finally came into force on January 12, 2017, and member states will have until January 12, 2019

to incorporate it into their national legislations. A notable advance in European employee benefits, the IORP II Directive encourages employer-funded retirement plans on a cross-border basis and introduces pensions fund transfer procedures between member states, making it easier for international companies to save more by consolidating existing pension schemes in different member states.

Since the U.K. will still be member of the EU in January 2019, IORP II will need to be incorporated into U.K. national law. However, the U.K. will have to negotiate a deal with the EU to benefit from IORP II after its exit.

### ***The Pan-European Personal Pension Product (PEPP)***

The European commission has launched a new voluntary personal pension scheme that allows employees to put money aside for retirement under comparable terms regardless of country of residence. PEPP will be portable in all EU member states and will give European residents more choices to complement their existing state pensions. It creates a single market for personal pension plans that can be offered by many financial services providers. PEPP will have the same tax treatment as EU member state pensions, and studies have shown it could considerably expand the personal pension market from €1,400 billion to €2,100 billion by 2030.<sup>20</sup> British financial firms wishing to participate in the PEPP market will have to establish themselves or a subsidiary within the EU. It is still unclear whether U.K. residents will be able to benefit from PEPP since it will be regulated by an EU institution. That will be part of negotiations.

The EU initiatives on employee benefits show that the departure of one member state and the other securities issues will not stop the EU from continuing to strive toward to a single capital market with the remaining countries.

### **EU Labor Regulations**

All EU laws in the U.K. will be affected by Brexit in the long term. When the U.K. effectively leaves the EU, the U.K. government can amend or repeal EU laws and related case law. Therefore, there is no guarantee on the continuity of EU employment or employee benefit law in the future. The EU employment law protections include a prohibition of discrimination based on age, gender, sexual orientation or religion and regulations regarding issues such as employment protection in business transfers, consultation rights, working time, holidays and other employee rights.

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Given the two-year time line before the U.K. leaves the EU and the time it will take to decide which EU laws to amend or repeal, it is likely that U.K. employees will continue to enjoy the same EU protections and benefits for several years to come. It is highly unlikely that the U.K. would make radical changes to these longstanding rights without fierce opposition from U.K. workers. Furthermore, many U.K. laws already guarantee employee rights regarding matters such as unfair dismissal, minimum wage, anti-discrimination and parental leave. However, some unpopular EU regulations are likely to be repealed or amended, such as agency worker protections and paid holidays for part-time workers.

### **A New European Workforce**

It may take several more years before the impact of Brexit on talent strategy and employee benefit plans in Europe can be accurately assessed. International corporations planning to relocate employees due to Brexit have many options and multiple countries to choose from; however, several EU countries are taking steps to ensure that they benefit from the U.K.'s uncertain fortunes and successfully compete for its financial services jobs and departing talent. France, Germany, Ireland and Italy have all made recent changes in tax and labor law to make their countries more attractive to highly skilled workers and multinational employers, but continental European countries tend to be more protective of employees and have greater employee consultation requirements and employee benefits mandates under national and industry collective agreements. Human resources will need to familiarize themselves with the unique talent profiles, employment law and labor cost structures in these other European markets where they may soon have growing numbers of employees. 🌐



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