The Highland Council

29 June 2016

Agenda Item	
Report No	HC/33/16

UK European referendum and its implications for Highland

Report by Chief Executive and Director of Development and Infrastructure

Summary
This report attempts to identify some of the impacts that are likely to arise from the UK decision to leave the European Union. It describes a number of areas where Highland is supported financially by the UK's membership of the European Union.

1. Introduction

1.1 The result of the 23 June referendum has seen a majority vote in favour of the UK leaving the European Union (EU). The formal process of leaving the EU is triggered by the UK government invoking Article 50 of the Lisbon Treaty, thereby commencing a period of formal negotiation of the terms of withdrawing. Membership of the EU would then cease from the date of entry into force of the withdrawal agreement, or failing that, two years after the notification, unless there is unanimous agreement with EU members to extend this period. While there is no legally defined timescale as to when (or indeed how) the UK government should invoke article 50, indications are that this would happen in autumn 2016 meaning the UK would leave the EU before the end of 2018.

2. Impact Analysis

2.1 The referendum result will clearly have an impact on the people, communities and businesses of the Highlands as well as on the Council and its public sector partners. In the current rapidly evolving situation it is impossible to be specific about what all these impacts will be but a number of areas where the impacts could be significant are detailed in this report and appendices.

2.2 The report at **Appendix 1** is a Briefing by the Association for Public Sector Excellence (APSE). It is specifically focused on implications for local government and highlights issues which will be of particular reference to our sector.

2.3 The report at **Appendix 2** has been prepared by Ernst Young LLP and offers broader insights into process, timetable, key drivers and government policy.

2.4 Members will recognise that while these reports are informative they pose more questions than they answer. The answers will develop over the coming weeks, months and indeed years.

3. European Funding Issues

3.1 The Highland area and the Council itself benefits from European Structural Investment Fund (ESIF) programmes. Highland gains some benefit from a number of national programmes but more significantly is the beneficiary of a number of programmes delivered at a Highland or Highlands and Islands level. These ESIF programmes comprise the:

- European Regional Development Fund (ERDF)
- European Social Fund (ESF)
- European Agriculture Fund for Rural Development (EAFRD)
- European Maritime and Fisheries Fund (EMFF)

Allocations are made for the Highlands & Islands and for ERDF and ESF these are quoted in Euros as the partnership agreement between the EU and then UK underpinning these are in Euros. Once these allocations are translated into specific Scottish Government programmes they are converted into sterling and Lead Partners enter into contracts with the amount committed quoted in Sterling. In recognition of the current volatile exchange rates, figures quoted in this report follow this protocol to avoid giving misleading figures. **Appendix 3** details the levels of funding which are involved.

3.2 The European Regional Development Fund helps fund initiatives such as business support, financial instruments (loans, guarantees etc.), low carbon, green travel, waste reduction and IT including the rollout of next generation Broadband. There is an allocation of €141m for this programme in the Highlands & Islands.

3.3 The European Social Fund helps fund initiatives such as vocational training, employability measures and poverty reduction. There is an allocation of €51m for this programme in the Highlands & Islands.

3.4 The European Agriculture Fund for Rural Development provides agriculture support and support for rural development including LEADER. EAFRD is delivered as the Scottish Rural Development Programme (SRDP) and has no specific Highlands & Islands allocation. There is an allocation of £8.8m for the LEADER programme in Highland with a further allocation for the Cairngorm National Park.

3.5 The European Maritime and Fisheries Fund supports measures for the fishing industry, port infrastructure and community development. EMFF is a UK wide programme, again with no specific allocation for the region. However, the Community Led Local Development (CLLD) element has an allocation of £0.7m in Highland.

3.6 The Highland Council is the Lead Partner for three Structural Investments (SIs) using the above programmes :

- Business Competitiveness (Business Gateway) £ 1.18m
- Employability £10.34m
- Social Inclusion & Poverty £ 1.42m

and is in the process of applying for funding as a delivery agent in two projects where another public sector partner is the Lead Partner. In a number of cases the Council delivers these services through Third sector partners who would see a negative impact if such funding was ceased.

3.7 In addition to ESIF, Highland has access to 42 other transnational and transregional programmes and a number of these are accessed by Highland Council or its partners. Key amongst these are:

- Horizon 2020 (the EUs Research and Innovation programme with a budget of nearly €80 billion for 2014 to 2020) – being accessed by the Council along with HIE and UHI;
- Erasmus+ (the European Union programme aimed at modernising and enhancing education, training, youth work and sport) – primarily used by the Care & Learning Service;
- Interreg – programmes to promote harmonious economic, social and territorial development of the Union as a whole which are built around three strands of cooperation:
  - cross-border (Interreg A) – For Highland this is limited to the Programme with the ROI and NI;
  - transnational (Interreg B) – Includes four programmes accessible in Highland (Northern Periphery & Arctic, North West Europe, North Sea and Atlantic Area); and
  - interregional (Interreg C) – includes four Programmes under the INTERREG V C 2014-2020 banner, all accessible to Highland.

3.8 In the short term, participation in these European funding programmes will continue while withdrawal from the EU is negotiated. The Scottish Government has already indicated to a number of partners that there will be no immediate change to Scottish 2014-20 ESIF programmes and that any funds already committed will be administered as usual. Withdrawal of any of these funding programmes in future would have a significant detrimental effect on Highland.

3.9 In addition to the above funding programmes which essentially support “one off projects”, agricultural businesses including farms and crofts are recipients of funding through the EU’s Common Agricultural Policy (CAP) payments. The CAP implements a system of agricultural subsidies on which production and many agricultural investment decisions depend so any withdrawal of these is likely to be detrimental to the sector. In recent years there has also been an increased emphasis on linking CAP payments to positive environmental management which could also be affected with any withdrawal of funding.

4. Other Key Issues for Highland

4.1 <u>EU nationals living in the Highlands & the Highland workforce</u>
Highlanders have always warmly welcomed people from other countries who choose to live and work in our area and it will be important at this time to provide reassurance to EU nationals that this welcome continues and that we value their contribution to Highland life.

Highland is home to a large proportion of migrant workers (and their families), notably those from EU countries. Exact numbers are not available and while an earlier quoted figure of 10,000 in 2011 was considered high, subsequent growth allied with the Office for National Statistics estimate of 15,000 non UK born residents in Highland in 2014 suggests this figure is now likely to be fairly accurate. This diversity and the importance of EU migrants to the economy is well illustrated by those attending a recent two day start up workshop for Business Gateway in Sutherland - attended by 8 people there were 2 French,1 Hungarian, 1 Pole, 1 Australian and 1 Canadian as well as 1 each from Scotland and England.

A number of sectors including agriculture, construction, fish and food processing and hospitality have previously struggled to recruit staff at times and in more recent years many businesses in those sectors have been dependent on EU migrant workers. The NHS and care sector in the Highlands are also reliant on EU and overseas workers although no precise figures exist locally.

4.2 Inward Investment

Highland and the UK as a whole benefit from inward investment by international companies who often use the UK as an entry point for accessing European markets. Any changes to the single market arrangements that introduced barriers to trade as well as economic uncertainty and currency fluctuations could make Highland a less attractive place to invest.

4.3 Exports

A number of Highland businesses are dependent on exports with the EU being a core market for many of them. Most notable are the Food & Drink sector – which incorporates the whisky and salmon farming industries. Highland figures are not available but figures for Scotland as a whole show 43.4% of exports were to the EU (2014).

4.4 Tourism

Levels of inbound tourism to the Highlands are influenced by a number of factors including exchange rate variations. Should the current situation of a weaker pound continue the most likely outcome would be an increase in the number of overseas visitors and an increase in domestic visitors who would now find it more expensive to travel overseas. The perception that the referendum result might give as to how welcoming a place the UK is, may however negatively impact on the number of European visitors. Bearing in mind the fact that international visitors are considerably higher spenders that domestic visitors, any future reduction in international visitors could still have a detrimental effect.

4.5 Procurement

The Highland Council is in the process of tendering for the delivery of services funded by European programmes and further tenders are expected for future activity. Uncertainty over the time EU funding programmes will cease in Scotland creates a further level of risk in entering into any such contracts that will require to be managed.

4.6 Impact on Partners

The Council's public sector partners benefit to varying levels from EU funding, networks and the free movement of labour. Each will no doubt be reviewing the impact of Brexit on their interests and it will be helpful to use the forum of the Community Planning Board to develop a comprehensive analysis of the overall impact on the Highlands.

5. Next Steps

5.1 At this stage it is recommended that the Leader invites interested Members and key Officers to an early meeting to consider possible scenarios and initiate the development of contingency plans to mitigate the most significant risks. Follow-up meetings can be convened on an ad-hoc basis.

Recommendations

Members are invited to note the expected implications for Highland of the UK decision to leave the European Union and to meet as appropriate to consider possible scenarios and initiate contingency planning.

Designations: Chief Executive
Director of Development and Infrastructure

Date: 27 June 2016

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Appendix 1

Briefing by the Association for Public Sector Excellence (APSE)
Brexit: Implications for Local Government

Appendix 2

Ernst and Young LLP Report
Impact of Brexit on the Government and Public Sector

Appendix 3: Allocations from 2014-20 EU programmes

Allocations to Highlands & Islands from the ERDF/ESF Programmes (quoted in Euros as the partnership agreement underpinning these are in Euros only).

Strategic Interventions (2014-20)		Amount Million €
Innovation	ERDF	€ 15
Scotland's 8th city – The Smart City	ERDF	€ 2
Business Competitiveness & Financial	ERDF	€ 35
Next Generation Broadband	ERDF	€ 25
Developing Scotland's workforce	ESF	€ 29
Low Carbon transport and Low Carbon Infrastructure Transition Development Fund	ERDF	€ 26
Resource Efficient Circular Economy Accelerator	ERDF	€ 7
Green Infrastructure	ERDF	€ 2
Enhanced Employability pipeline	ESF	€ 26
Social Inclusion and combating poverty	ESF	€ 25
Total		**€ 192**

The following are the actual amounts applied for under the three Strategic Interventions the Council is leading. Figures are given in Sterling in accordance with our actual applications:

Strategic Intervention (2016-18)	Amount Million £
Business Competitiveness (Business Gateway)	1.18
Employability	10.34
Social Inclusion & Poverty	1.42

In addition the Council is applying for operational activity from the following Strategic interventions as a Delivery Agent:

Strategic intervention (2016-18)	Amount Million £
Scotland's 8th City (Glasgow lead)	1.8
Green Infrastructure	2

Highland SRDP Programmes (2014-2020)	Amount Million £
Highland LEADER Programme	8.8
Highland EMFF (CLLD element)	0.7

CAP 2014-20	Amount Million €
Pillar 1 (indicative PA for Scotland)	580
Highland share (estimated at 6%)	34.8
Pillar 2	478
Highland share (estimated at 6%)	28.68
Total	**63.48**

apse membership resources

Briefing 16-21 June 2016

Brexit: Implications for Local Government

Key issues
This briefing explores the implications of the UK vote to leave the EU. Specifically we explore:- • What 'Brexit' will mean for local authority trading companies, procurement, environmental protection issues, municipal energy and workforce matters as well as budgets and investment matters such as housing. • As further details emerge on the negotiations APSE will provide additional briefings to its' member authorities.

1. Brexit: what happens next?

Following the referendum vote the political fall-out has been dramatic leading to David Cameron's resignation as Prime Minister. This means that article 50 of the Lisbon Treaty, which is the route to trigger an exit from the EU by any member state, is highly unlikely to commence until a new Prime Minster has been appointed (by Her Majesty the Queen). In accordance with Parliamentary Protocol this means the majority party, the Conservative Party, will elect a new leader who will then be presented as the Prime Minster; It is possible that calls for this to trigger a General Election will gain traction but so far this is by no means a certainty. If the new PM is 'appointed' then that person will be responsible for the initial trigger of Article 50. The EU could not force the trigger of Article 50 on the UK.
Article 50 is as follows:-

1. Any Member State may decide to withdraw from the Union in accordance with its own constitutional requirements.
2. A Member State which decides to withdraw shall notify the European Council of its intention. In the light of the guidelines provided by the European Council, the Union shall negotiate and conclude an agreement with that State, setting out the arrangements for its withdrawal, taking account of the framework for its future relationship with the Union. That agreement shall be negotiated in accordance with Article 218(3) of the Treaty on the Functioning of the European Union. It shall be concluded on behalf of the Union by the Council, acting by a qualified majority, after obtaining the consent of the European Parliament.

3. The Treaties shall cease to apply to the State in question from the date of entry into force of the withdrawal agreement or, failing that, two years after the notification referred to in paragraph 2, unless the European Council, in agreement with the Member State concerned, unanimously decides to extend this period.
4. For the purposes of paragraphs 2 and 3, the member of the European Council or of the Council representing the withdrawing Member State shall not participate in the discussions of the European Council or Council or in decisions concerning it.
5. A qualified majority shall be defined in accordance with Article 238(3)(b) of the Treaty on the Functioning of the European Union.
6. If a State which has withdrawn from the Union asks to rejoin, its request shall be subject to the procedure referred to in Article 49.

Accordingly from the point of Article 50 being triggered there will be a two year negotiation period, though this could be extended by agreement of the member states. In addition the Chancellor, George Osborne, has indicated that there would be no trigger under Article 50 until there is agreement about the outline of negotiations so in reality the two year timescale may be in fact much longer, allowing for the pre-negotiation period.

2. What will be negotiated?

Primarily the EU will remain a major trading bloc with the UK and as such there will be on-going interdependencies on matters such as freedom of movement, financial services, border controls and security, defence and of course the importing and exporting of goods and services. Therefore many matters that apply to the UK as a member state may continue to apply in one form or another even after a negotiated exit.

The negotiations will, by necessity, include tariffs and trade-offs. Many commentators believe that the EU will be inclined towards a 'tough line' in negotiations to deter other EU member states from contemplating exiting the union. Equally however the UK is a significant trading state and will have its own strong hand to play in the negotiations.

3. What are the main issues for local authorities?

Local authorities have become used to navigating and complying with EU directives in the course of its' day to day business, specifically in areas such as public procurement and employment law. For the immediate future nothing will change and the EU has already made it clear that it expects the UK to be compliant with EU law during the course of the exit strategy.

On the 24 June EU President Donald Tusk (the presidency is currently held by the Netherlands) issued a statement which included the following:-

"Until this process of negotiations is over, the United Kingdom remains a member of the European Union, with all the rights and obligations that derive from this. According to the

Treaties which the United Kingdom has ratified, EU law continues to apply to the full to and in the United Kingdom until it is no longer a Member."

Therefore in the short term there will be no slackening of compliance requirements and in any event many issues of compliance may remain in order to ensure the UK's position as a future member of the European Economic Area. The following provides a summary of issues across different areas of local government activity.

Procurement rules (including local authority trading companies)

There are the three sets of procurement Regulations including Public Procurement, Utilities and Concessions which will continue to apply across the UK (including Regulations recently brought into force in Scotland by the Scottish Government). APSE has already received a query from a member authority about what the exit vote will mean for 'Teckal companies', whereby external trading is limited to 20% by the EU Public Procurement Directive. The immediate answer is that nothing will change and in the longer term it will be a matter for UK Governments to decide whether or not they would wish to continue with regulations over public procurement matters, including public to public cooperation arrangements. Indeed these matters are also likely to form part of negotiations with the EU.

As the UK will want to ensure access to EU markets, as part of any future membership of the European Economic Area, or a free trade agreement, it is therefore highly unlikely that public procurement will become de-regulated, since the EU is likely to insist on the continuation of many of the regulatory measures. In any event the EU measures have been incorporated largely into domestic legislation so whilst there may be a need to update, to reflect the changing dynamics, it is unlikely that there would be a total dismantling of the procurement regime.

In addition there are also other areas of international regulation to which the UK is currently a signatory such as World Trade Organisation agreements on procurement. It is also unclear where the UK will place its' position on the issue of the Transatlantic Trade and Investment Partnership (TTIP). It is perfectly possible for the UK to attempt to continue as a party to TTIP outside of the EU, albeit TTIP has been a highly controversial matter for the UK and other EU countries.

Post the negotiations it is possible a very complex set of procurement rules will apply as part of the trading arrangements, and incorporation of new regulations, to ensure compliance with whatever is agreed within UK law. Consideration will also need to be given as to how these take effect in all four UK administrations.

Environmental regulations

Waste and recycling: Many APSE member councils are proactive advocates for better waste management and disposal. The EU is credited with driving forward and advancing recycling and waste management matters, and much of the UK legislation on waste and recycling was developed to reflect EU Directives. However there is cross-party political support within the UK on waste reduction, effective waste management, disposal and recycling so it is unlikely that current targets, for example on recycling, will be reduced or lessened. Indeed some UK administrations have already gone further than required by EU regulation, for example the zero waste targets within Scotland. However where our primary regulations relate back to EU matters then some legal amendments will be necessary to major pieces of UK legislation such as the ***Environmental Protection Act 1990*** which is a point of reference for many waste matters. In addition the aims and endeavours of the TEEP regulations will be an interesting point as to whether TEEP will be fully embraced in the absence of a 'push' from the EU.

Weed controls and chemicals: Many Parks and Public realm managers will be aware of EU compliance measures on weed control and the use of specific chemicals, including the ongoing debate on the use of glyphosate. Again whilst the source of regulations may emanate from the EU it is highly unlikely that there will be any realistic demands for deregulation of what is largely seen as public interest protection measures. Britain has shed its 'dirty man of Europe' label through vigorous pursuit across measures to improve environmental quality and there will be little support or appetite amongst policy makers to travel backwards on environmental policies.

Carbon reduction: Whilst there are European targets on climate change and emission reduction targets the UK has its own Climate Change Act 2008, and is also a signatory to the Kyoto Protocol (since 1995) as well as many other domestic and international carbon reduction commitments. Again given the global nature of environmental matters it is unlikely that we would see a lessening of targets. By the UK maintaining its commitment on climate change matters these are reciprocated by other countries, EU or otherwise, and as such the UK would remain a beneficiary of reciprocal arrangements.

Housing and construction

Recent APSE and TCPA research on housing suggests that the UK needs to reach at least 250,000 new homes each year for sale or rent to meet housing demands (which could rise to 330,000 new homes should new house-building be delayed). So far the UK housing need is predominantly being met by private house builders and developers, with APSE calling for a much stronger role for local councils in building new council homes.

In the immediate aftermath of the referendum vote a number of housing developers saw their shares values slump, rapidly declining by around 25%. Any pull on the share values of developers could make the UK a less attractive investment option and hence create a lessening of new build schemes and projects. This will be unhelpful to local authorities (and Combined Authorities) in terms of housing strategy and housing developments. Whilst this situation may stabilise once markets recover, in the realisation that the immediacy of

Brexit will be a managed and negotiated process, it will nevertheless make the housing and construction market nervous.

In *'Homes for All: Ensuring councils can deliver the homes we need'* APSE has explored the development of wholly owned local housing companies which have some significant advantages for local authorities, in terms of the speed by which new developments can be delivered, and sharing of risk. An APSE event exploring options for delivering new homes including local housing companies, owned by local authorities will be held in Leicester on the 8th July.

APSE would urge councils to take all necessary measure to continue to develop solutions to housing need in local areas.

Energy

APSE Energy works with local authorities on the municipalisation of energy markets with a focus on renewable energy and income generation from renewable energy. It also provides support and guidance on energy efficiency measures.

In terms of energy markets it is too early to say what the likely implications of Brexit will be but APSE Energy will be keeping a watchful eye on whether the UK chooses to remain within the Internal Energy Market. Europe has been pushing for greater transparency and regulation in the energy markets but many UK local authorities remain concerned about levels of fuel poverty amongst households. Accordingly, an increasing number of local authorities, have taken matters into their own hands by developing ESCOs (local authority energy services companies). Any new regulatory requirements, at a domestic level, should therefore in APSE's view maximise the flexibility for local authorities to create and embed local energy solutions.

Targets, such as 15% of energy coming from renewables under the EU Renewable Energy Directive are likely to remain. Indeed this issue was stated as the remaining intention of Government even when domestic changes to renewable tariffs and tops ups were introduced in 2015 and in early 2016.

Workforce matters

A range of matters will impact upon workforce issues as many domestic employment matters emanate from the EU. That being said it would be wrong to imply that there is co-dependency on the EU as, even where legislation has been drawn down from the EU, it has largely been brought into domestic law by way of Acts of Parliament. It would therefore need to be withdrawn domestically which would be unacceptable to many on a cross-party basis. Where employment rights are potentially weakened is where there is an appeal to the European Courts on points of interpretation, with reliance on the original wording in the specific EU directive. In the longer term however it is likely that pressure will build from industry on the arguments of 'employment red tape' and it will be essential to have a mature debate on the necessity and impact of employment matters rather than a reactionary approach.

A key area of impact will be on freedom of movement and EU labour laws allowing EU workers to work across member states. Whilst employers are already obligated to make checks on the status of workers we may see a tightening of requirements, post exit, and dependent upon what form worker movement takes. Retaining some freedom of movement is highly likely as part of the European Economic Area (EEA) and therefore new compliance measures on employers, including local councils as employers, will be inevitable. For now however there are no immediate changes on the horizon.

APSE comment and conclusions

APSE would suggest that unless otherwise directed local authorities should continue with their existing compliance measures and should not assume any lessening of the risk of challenge for non-compliance on EU matters.

There are some emerging concerns on matters such as the EU infrastructure funding for large scale projects, such as HS2 and transport projects, alongside the possibility of further fiscal tightening, should the economy start to rapidly contract as a result of Brexit. Additionally concerns have been raised as to the future financing of Combined Authorities and City Deals. However the Chancellor has stated (on the 27 June 2016) that there will not be an emergency budget for the time-being; local authorities will however no doubt be nervous of any future funding challenges presented as a result of the EU vote.

APSE is also concerned that the negotiations surrounding the UK exit should not be conducted in a vacuum. Interested parties across the economy should have the opportunity to voice their concerns or demands of Government before decisions are made, both in the pre-Article 50 period and post the formal Article 50 trigger. APSE would urge the formation of a cross sector local government forum to ensure, that as well as strategic matters for local government, the interests of those providing frontline local government services are effectively represented. APSE would wish to avoid local councils ending up with unintended consequences for local council services.

Over the coming months, and as matters develop further, APSE will be informing and advising our member councils through our advisory groups, commercialisation network and regional events of developments in the negotiations. We would also be pleased to receive comments, questions and suggestions from our member local councils about specific matters so that we can investigate these points further and formulate a response as issues emerge. Please email mbaines@apse.org.uk with your suggestions.

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EU Referendum: Impact of Brexit on the Government & Public Sector (GPS)

27 June 2016

Building a better working world

Macro summary of impact on the Government & Public Sector (GPS)

The 'Leave' vote will lead to a significant impact for the public sector as it will be the sector that has to deliver the implementation of Brexit and experience leadership change. We now know that there will be a change of Prime Minister. In addition it is possible that an opposition leadership context will also take place in the near future.

With parliamentary recess approaching the majority of activity is now likely to be taking place outside of Parliament until the Autumn. Public sector business and service delivery will continue across the full breadth of the sector, but public servants within departments and beyond will be awaiting to understand what the political fallout will mean for them and their work.

Over the Summer the leadership contest will run its course whilst in Whitehall the civil service starts to plan for the process to leave the EU. Immediate impacts are likely be a significant distraction effect within central government as a new political leadership team comes to grips with the decision to leave and the 'promises' made to the electorate of the benefits of leaving at a time when the economy could suffer a material blow. Wider political impacts will be felt if the devolved administrations (Scotland in particular) continue to push for further referendums. This will likely lead to further instability in terms of the make up of the United Kingdom.

The UK Government will feel under pressure to start delivering palpable signs of the promised benefits whilst tackling the real task of the economy and negotiating exit from the EU. The negotiation will place a large burden on the likes of Cabinet Office, HMT, FCO, BIS and the HO and will likely distract from the normal run of business - this will spread to other departments as the task of unpicking legislation progresses.

The UK has not had a trade negotiation capability of any note since the 1970s. EU legislation has been embedded in UK law and built upon over forty years of regulations, directives and agreements blurring the legislative lines between the UK and EU. The government needs to decide how to opt out of each element and what alternatives will be put in place – stated as being 80,000 pages of agreements. Likely to tie up parliamentary time for years unless wholesale acceptance and targeted action is taken.

Macro summary of impact on GPS (cont'd)

This distraction and any remedial measures to tackle the economy will dominate parliamentary time for a considerable time and, in the short term, could delay decision making on current government business such large programmes currently in train.

Particular claims during the Leave campaign have been more money for the NHS, reduced taxes on such things as utilities, protection of regional and agricultural grants, fisheries policy and controlled immigration/improved border controls. All of these would take government time and attention and cost money at a time when the economy could take a sustained downturn post vote impacting upon such targets as house building and seeing investors move temporarily or permanently away from the UK.

However, it is unlikely that the disentangling of UK/EU legislation can take place quickly enough for UK contributions to be reduced materially in the next couple of years. The electorate are also likely to expect quicker results and therefore it is highly likely that the new political leadership would need to revisit the announcements in SR15 and effectively redo the spending review (say in autumn 2016 or post a general election if one happens in 2017). The process of a spending review itself and the uncertainty within government of the outcome could lead to a further dampening of activity for several months as seen post 2015 election.

One of the key issues will be dealing with the many complex challenges over an extended period of time that need the civil service to sort and deliver them. As the political situation settles then leaving the EU will become a reality with its own operational, administrative and political challenges. The civil service will need to continue to successfully deliver government business in a context of increased and extended political uncertainty.

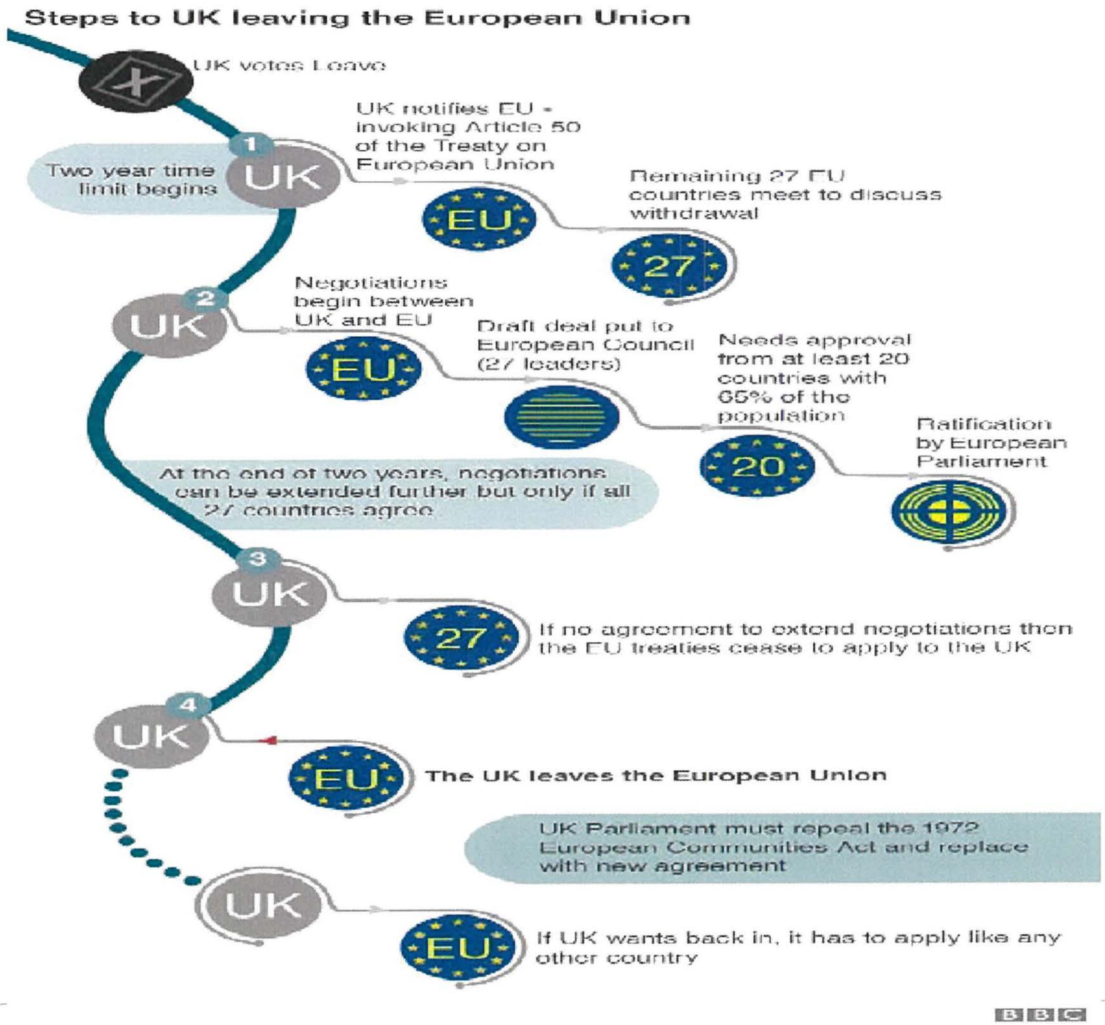
The Chancellor's speech on the 27 June 2016 summed up the key risks - market volatility is likely to continue, uncertainty will impact investment, and there is a long way to go to agree future long-term economic relationships.

Key next step dates

- **28 June** - EU leaders are due to gather for a summit in Brussels.
- **1 July -** the Netherlands will hand over the EU's six-month rotating presidency to the relatively-inexperienced Slovakia, which must now lead the negotiations towards Brexit. The UK had been due to take the helm at the end of 2017, but that will not happen now.
- **21 July** – the Westminster Parliament is due to rise for its summer break, but the civil service and ministers will need to continue to work on preparations for negotiations.
- **Mid August** - if the Conservative leadership takes a similar length of time as in 2005, this is around when the successor to Mr Cameron could be announced. Given the need for someone to take charge of the talks, It is likely there would be a strong desire to move as fast as possible. The new PM would then presumably set out their reshuffled cabinet before Parliament returns.
- **5 September** - Parliament is due back for 10 calendar days, and while the early Autumn sitting is usually quiet, this year it could be extremely busy as the government tries to reduce the backlog of business. It is not certain that any Brexit related legislation will be brought into this session.
- **15 September – 10 October** – Conference season. This will be the opportunity for the new PM to set out the vision and timetable for Brexit.
- **Mid October – 20 December** – Autumn parliamentary session – this will the first real opportunity for Parliament to focus much time and attention on Brexit related legislation.

EY

Key process & Timeline steps
(source BBC)



EY

Key EU legislation focus

Operations | Employment | Consumer protection | Data retention | IP | Health & Safety | Environment

EU legislation in all its forms touches all parts of the GPS sector by the nature of the market covering all aspects of UK life. Vote Leave has called for legislation in the current session of Parliament to 'end the European Court of Justice's control over national security and allow the government to deport criminals from the EU'. The Brexiteers have also pledged to abolish the 5% rate of VAT on household energy bills by amending the VAT Act 1994. Other parliamentary actions promised by the Leave campaign include ending the automatic right of all EU citizens to enter the UK, and repealing the European Communities Act 1972 (Repeal) Bill - the legislation that guarantees the supremacy of EU law to domestic rules.

However, it is clear that it will take some time to cut the ties to Brussels. Based on the focus issues of the Vote Leave campaign key areas of legislative focus over the coming months/years for the government are likely to be:

- Finance Bill – to respond to any economic shocks via an emergency budget/autumn statement
- Overall disentangling of EU legislation – upon which much UK legislation has subsequently been built upon so no small task
- Devolved Administrations – Second Independence Referendum in Scotland?
- Immigration/border controls/policing
- Defence/security arrangements
- Trade deals and business regulatory laws,
- Agricultural & fisheries policies
- Taxation
- Energy
- Devolution/local government
- Transport – for instance a new runway could be seen to be critical to expanding the UK's trade.

Scenario drivers

Trade

Exports to EU, access to markets, imports (supply chain) from EU, impact on customers, e.g. business done in UK with EU-owned businesses; NB trade with other markets could also be impacted as EU trade deals are taken away from the UK

Risk area	Summary of impact / possible preparatory steps
1. Trade deals (EU)	• The UK would need to start negotiations for new trade deals with the EU – this is likely to be protracted and potentially hostile, and will require significant civil service resource and legal advice. This could introduce uncertainly into the business world and markets and be a significant distraction for government. • Coupled with this will be the lack of trade negotiation in the UK government – no real capability has existed since the 1970s although there are UK civil servants with experience of negotiating on legislative issues within the EU.
2. Trade deals (non EU)	• Following a leave vote the UK will be free to negotiate trade deals outside of the EU. This would also be a priority for the government as it is a visible sign of the benefits of Brexit whilst helping support the economy. • But this may not be able to be accomplished in an accelerated timescale and would require capable civil, service resource – which government does not have in swathes as most negotiation has been carried out by the EU and negotiating a new deal with the EU could be prioritised over non EU deals. • It is also not clear that such negotiations can be legally formalised before the UK formally leaves the EU.
3. Energy	• Impacts could well be seen in utilities and power as many are owned/operate by European HQ companies e.g. EDF, EoN, Scottish Power etc. and issues could relate to debt leverage, corporate structure, future funding e.g. Nuclear New Build – Hinkley Point C. • Power trading could also be impacted - e.g. import/export agreements between National Grid and France.

Scenario drivers
Trade (cont'd)

Exports to EU, access to markets, imports (supply chain) from EU, impact on customers, e.g. business done in UK with EU-owned businesses; NB trade with other markets could also be impacted as EU trade deals are taken away from the UK

Risk area	Summary of impact / possible preparatory steps
4. Local government	• Local authorities and enterprise agencies are central to driving the growth of the economy in supporting balance of payments in their localities. There will be a high level of uncertainty for businesses to invest and recruitment following the immediate impact of Brexit that may productivity and trade and major issues. • Companies may stop UK plans to locate in the UK set up sites elsewhere. FDI could be reduced as many companies locate in the UK to trade with Europe • Tariffs will clearly be an issue –it will certainly be a question businesses will want answers to quickly but will take time. • With regards to devolution it may be difficult for the government to reverse the trend as the mantra of the Leave campaign has been to 'take back control' and have self determination – likewise this will make it difficult for a Brexit focused government to resist pressure from the devolved administrations to have more say in their affairs or to hold referendum on ceding from the UK.
5. Carriers	• Airports – impacts on operators regarding air space and landing agreements will cascade into airport owner/operators with respect to future expansion (new runway) Visa and travel impacts likely to significant impact on sector e.g. low cost airlines.
6. Business Uncertainty	• Companies may stop plans to locate/invest in the UK and set up sites elsewhere. FDI could be reduced as many companies locate in the UK to trade with Europe. Tariffs will clearly be an issue –it will certainly be a question businesses will want answers to quickly but will take time to resolve introducing more uncertainty.

Scenario drivers
Migration

Impact on ability to hire skilled and unskilled staff, possible wage pressure, impact on existing staff

Risk area	Summary of impact / possible preparatory steps
1. Health	• The NHS relies heavily upon migrant workers both professional and semi skilled. Any changes to immigration policy may impact upon the NHS and social care services' ability to delivers services.
2. Local Government	• Migration is always an issue for Local Authorities who are usually the end point for housing and location of migrants to the UK as well as employing large numbers in social care. Changes may create issues of access to capabilities and labour. • Could be a movement of companies locating elsewhere over the medium term to access broader EU workforce market creating local issues of investment.
3. Infrastructure	• Potential large impact upon the EU migrant labour workforce needed to deliver infrastructure programme across all sectors. Infrastructure also use large migrant workforce for maintenance and operating assets.
4. Higher education	• The UK education system is highly dependent upon non UK students to help fund the overall system,. With Brexit this could change and reduce the amount of income coming into the system and putting the HE system under greater pressure. • The sector is already gearing up/entering a period of consolidation without any Brexit impact.

Scenario drivers

Regulation

Changes to regulation of products and services, impact on standards and future investment

Risk area	Summary of impact / possible preparatory steps
1. **Business regulation**	• Brexit will allow the UK government to reduce business regulation and 'red tape' however the likelihood is that in order to trade with the EU the UK would still have to abide by EU regulations to a large degree. • There are areas such as environment regulations, Employment law and the Working Time Directive that have to be questioned as to whether or not these are seen as 'bad' legislation. Reducing red tape could make the UK more attractive to external investment but the attraction of the larger EU market could attract movement of companies from the UK to the EU. • A reduction in red tape, if it affects workers rights, could also potentially lead to a resurgence in trade unionism.
2. **Local government**	• Legacy funding and investments from previous EU projects are now maturing and subject to EU rules. This may change. Many regions are subject to grants /debt funding supported through the EU. There will even be more uncertainty as the rest of the world may not continue to trade with the EU on the same basis when we are no longer part of the 'club'
3. **State Aid**	• When the UK leaves the EU, the rules preventing unlawful State Aid would cease to apply to the UK and Government would be in a position to revise their public spending guidelines and protocols. This could enable direct investment in certain projects that may not currently be possible due to the state aid rules. • This would have an obvious impact on such bodies as UKTI, Highlands & Islands Enterprise and Scottish Enterprise. The future model could be a more flexible model to work within, however following an expected negative impact on GDP post Brexit, there may be reductions in the amount of state aid made available overall and there are risk of trade tariffs being imposed.

Scenario drivers
Government policy

Access to EU research funding, taxation, possible use of state aid by UK Government to back selected sectors. *In addition to previous comments regarding Government policy the below are some specific issues of particular interest to the GPS market*

Risk area	Summary of impact / possible preparatory steps
1. General macro EU leave policy	• The government may feel under pressure to start delivering palpable signs of the promised benefits whilst tackling the real task of negotiating exit from the EU. The negotiation will place a large burden on the likes of Cabinet Office, HMT, FCO, BIS and the HO and will distract from the normal run of business - this would spread to other departments as the task of unpicking legislation progresses. EU legislation has been embedded in UK law for 40 years and subsequently built upon, so a complicated task unless EU law is accepted as UK law.
2. Re-visiting current spending policy	• Particular claims during the Leave campaign have been more money for the NHS, reduced taxes on such things as utilities, agricultural & fisheries policy, local government grants and controlled immigration/ improved border controls. All of these will cost money and government time at a time when the economy may take a sudden downturn post vote and investors move temporarily or permanently away from the UK. • It is very possible that the new political leadership would need to revisit the announcements in SR15 and effectively redo the spending review (say in autumn 2016). The process of review itself and the uncertainty within government of the outcome could lead to a further dampening of activity for several months as seen post 2015 election.
3. Public procurement	• The UK is subject to the EU Procurement Directive which has been adopted into UK law via enabling legislation: the Public Contracts Regulations 2015 in England and Wales, and the Public Contracts (Scotland) Regulations 2015 in Scotland. Nothing would change in the short term however these laws could be revoked and/or replaced with alternative legislation. The UK could restrict competition to the UK, but then it would be likely that the EU would also be able to restrict competition across the remainder of the EU to exclude UK businesses. The UK is however also party to the World Trade Organisation's Government Procurement Agreement however and, as such, even in the event of a Brexit, those rules would continue to apply.

Scenario drivers

Government policy (cont'd)

Access to EU research funding, taxation, possible use of state aid by UK Government to back selected sectors. *In addition to previous comments regarding Government policy the below are some specific issues of particular interest to the GPS market*

Risk area	Summary of impact / possible preparatory steps
4. EU grants	• The public sector currently benefits from grant funding from various EU institutions and that funding can be useful in research, stimulating growth and regeneration in areas and projects that would not otherwise be feasible. When the UK leaves the EU, it is likely that UK public sector bodies would no longer be entitled to apply for that grant funding, which may prejudice the ability to progress those projects or areas of research. This is particularly relevant to the LG and HE sectors. • We could also see potential reduction on locational grant funding for employment and infrastructure in the more remote/deprived areas such as the Welsh valleys, Highlands and Islands. These areas currently receive a higher % of European grant funding and this may not be able to be replaced by the relevant government. •
5. Local Government	• LEPs are heavily funding through Local Growth Deals and with a significant notional allocation or ERDF/ESF funding from Europe. This poses a risk and level of assurance as to what commitment of funding will remain and when it will expire. Will Government re-commit or be able to afford to re-commit to such funding? • Many local authorities are accelerating business support through significant borrowing through the EIB. Terms may change going forward and level of risk scrutiny could increase with ex-ante assessments. • A new industrial policy for key industries and sectors will need to be rolled out asap to bolster confidence and support, but on what basis? • Local government funding will be under scrutiny once again.
6. Higher Education	• HE sector relies heavily on EU students more than non–EU students. The UK may seem less attractive and lose income.

Scenario drivers

Government policy (cont'd)

Access to EU research funding, taxation, possible use of state aid by UK Government to back selected sectors. *In addition to previous comments regarding Government policy the below are some specific issues of particular interest to the GPS market*

Risk area	Summary of impact / possible preparatory steps
7. Accounting treatments	• Public Sector bodies in the UK are currently required to comply with the European System of Accounts 2010. These rules have impacted on the public sectors ability to structure finance solutions and delivery models. • Following Brexit the UK would no longer need to follow rules prescribed by Eurostat and that may allow the ONS to follow alternative accounting rules which could impact future delivery models.
8.. Infrastructure	• Uncertainty over the economy may restrict government's investment in infrastructure projects. This could couple with a perfect storm as investors are unwilling to invest in the UK and the fact that the European Investment Bank (the EIB) provides a large element of finance for many of the UK's largest complex infrastructure projects. 2015 saw a record year for the EIB's engagement across the United Kingdom • A Brexit will likely to impact on the UK public sector's ability to secure EIB finance, although it is also possible that a Brexit could give rise to alternative models.

Key immediate questions…

- What is the impact of a steep fall in sterling on your organisation?
- Do you have the capabilities to meet the challenges heading your way?
- Are you confident you can maintain service delivery through an extended period of uncertainty?
- Are there any risks to supply contracts, including outsourcing, as a result of the vote?
- What are the plans to retain the workforce, both skilled and un-skilled, now potentially at risk of losing their right to work in the UK?
- Have you communicated with staff?
- Are there any major bids outstanding or programmes underway that could be impacted?
- Are there any immediate issues relating to EU funding or projects such as R&D?
- What is the plan to manage the longer-term impact?
- Are there any opportunities your organisation could take advantage of during this period?
- Are you comfortable in the strength of business relationships with non-UK based distributors, customers and suppliers?
- Are you comfortable with your financing given the risk of interest rate rises to bolster sterling and a likely re-rating of the risk profile of UK assets?

EY | Assurance | Tax | Transactions | Advisory

Ernst & Young LLP

ED None

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