



# Preparing Brexit

## *The scale of the task left for UK business and government*

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### Summary

With just six months to go until the 31 December 2020 deadline, the UK is still not ready for the end of the transition period, when the new relationship between the UK and European Union (EU) – whatever form it takes – begins. Although the UK government has been preparing for Brexit since the 2016 EU referendum, there is still more to do. Some of these preparations will depend on whether an agreement on the future relationship is reached, and what it covers.

But whatever deal is – or is not – reached between the UK and EU, leaving the single market and customs union will impact nearly all sectors of the UK economy. The government will have the freedom to manage domestic policy in areas previously set at the EU level. But exercising that freedom will add friction to the trade in goods and services with the EU, which will still be the UK's largest trading partner by far. Freedom of movement will end, making it more difficult to travel to – and live in – EU member states and, in turn, risking labour shortages in some sectors in the UK. And the UK will lose access to part of the EU's toolbox of measures for co-operation across justice and home affairs.

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January will bring sweeping changes for the UK's public, as well as its government and business. But this paper focuses on the scale of the task facing government and businesses, on whom the responsibility for getting ready for the changing trading relationship firmly rests. We conclude:

- **The coronavirus crisis has made a difficult task much harder.** Since the pandemic took hold in February, and with the formal lockdown taking effect in late March, government and business resources have been focused on responding to the pandemic, rightly prioritising this over Brexit preparations. Firms reeling from the economic consequences of coronavirus are poorly placed to prepare for Brexit: in many cases, in a worse position than in the months leading up to the potential no deal in October 2019. As the government's own data shows, the majority of firms have not even begun to prepare.<sup>1</sup>
- **Continuing uncertainty about the future relationship has also hindered preparations.** There are still fundamental differences between the UK and EU on what they want a final agreement to look like. Until the shape of a deal is clearer, or the parties walk away from the talks, business cannot be clear exactly what it is they must prepare for – making detailed preparations impossible. Ambiguity and delay over the unilateral decisions the UK and EU will take after January (in either an agreement or no-agreement scenario), and what measures they may put in place to mitigate possible disruption at the end of the transition period, have also hampered preparations for business. Clarity and detail are needed to make real progress.
- **Preparation will not avoid disruption.** The scale of the changes in the trading relationship between the UK and EU – whether an agreement is reached or not – means that it will take time for businesses to adjust to the new conditions. And the government will need to be ready to respond to unforeseen disruption, too. In the longer term, the new friction involved in trading with the EU may make some businesses unviable – or create opportunities in other sectors – resulting in changes to the economy. How this will interact with the economic consequences of the coronavirus crisis remains to be seen.
- **Brexit does not end on 1 January 2021.** Some aspects of a deal could take several months, or even years, to be implemented fully, and negotiations on certain areas may also continue. Unilateral decisions taken by the UK or EU could, at a later point, alter the shape of the relationship and necessitate further legislative or practical steps to be taken by both sides. The UK will be adapting to the effects of Brexit for many years to come – which both business and government should be prepared for.

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As a result, the government should:

- **Target information and support to the least prepared businesses.** The government has now launched its latest Brexit communications campaign. A broad campaign will be necessary to ensure the public and businesses are aware that change is coming on 1 January 2021. But the government needs to ensure that the information available is clear and comprehensive – and provided in a ‘business friendly’ way. It must be particularly accessible to small and medium sized businesses that lack professional support and are least prepared. Not only do businesses need to understand what steps need to be taken, but also when they must act.
- **Build on the positive working relationship with business, much improved during the coronavirus crisis, to understand exactly what support is needed.** As we have found [in previous research](#), Brexit placed a strain on the relationship between government and business. But now that the UK has formally left the EU, the government needs to ensure it and business are in the best place possible to adjust to the inevitable changes at the end of the year. This should build on the close working relationships developed during the coronavirus response, such as regular meetings and frank exchanges of information.
- **Clearly communicate what mitigations or unilateral measures it will put in place, so that businesses know on what basis to make plans.** The government has recently changed its messaging on how businesses need to prepare for the GB–EU border: in February, businesses were told of the need to prepare for full checks from 1 January 2021, but now the government is planning on phasing in new border formalities over six months – although it has no control over the EU’s approach. There are other measures the UK government can unilaterally put in place to reduce the burden on business – such as recognising EU approvals. Making these decisions now, and communicating them to businesses, will give more certainty to industry as they start their preparations.
- **Take account of the impact of Brexit when finalising its economic response to coronavirus.** Brexit could end up compounding many of the issues businesses have faced in their response to coronavirus. The Treasury should include any anticipated economic shock as a result of Brexit in its planning for broader economic recovery, taking into account which sectors may be particularly under pressure.

Preparing for Brexit was always going to be a huge task. With just months to go, there is still much to do.

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## Introduction

Even before the coronavirus pandemic, getting ready for the end of the transition period was a huge task. Although the UK left the EU on 31 January 2020, the transition period meant that very little changed in practice.\* Government, individuals and businesses could largely continue to operate as usual. But on 31 December 2020, the UK is set to leave the customs union and single market, whether an agreement is reached or not. That date will usher in changes to the operation of the UK's border, new regulatory barriers to trading with the EU and the end of free movement.

With less than six months to go, the government faces an uphill struggle in ensuring the UK is as ready as possible for these major changes.

But it is not just the UK government that needs to be prepared for these changes. Getting ready is a team sport: it depends on the work of the devolved administrations, businesses and individuals. Without action from all, the UK will not be ready for Brexit. The EU also needs to ensure its citizens and businesses are ready for the changing relationship with the UK; it has already begun updating its preparedness notices – first issued to provide guidance to business and individuals in the run-up to a possible no deal in 2019 – accordingly.<sup>2</sup>

Both the UK and EU must also fully implement the Withdrawal Agreement by the end of the year, governing how some aspects of the UK–EU relationship will work beyond the transition period – including the border on the island of Ireland.\*\* Under the [Northern Ireland protocol](#), the UK government must be prepared to ensure that goods moving from Great Britain to Northern Ireland comply with EU rules on customs and regulation. The UK government is yet to fully explain how this will work, and be enforced, in practice.

There are also outstanding decisions both sides must make in the [joint committee](#), the UK–EU body established to oversee and monitor the application of the Withdrawal Agreement. Notably, these include the exact criteria for identifying goods deemed 'at risk' of entering EU markets and therefore subject to tariffs at the GB–NI border should the two sides fail to negotiate an agreement which removes tariffs.

Under the Withdrawal Agreement, the UK and EU member states also need to guarantee the rights of the UK and EU citizens who are living in the EU and UK, respectively, before the end of the transition period. The UK has made more progress here, already granting settled or pre-settled status to 3.46 million EU citizens in the UK.<sup>3</sup> Thirteen member states have chosen to implement an application scheme for UK citizens – but only three have actually begun the implementation (the other 14 are using a declaratory scheme, meaning individuals do not need to register to benefit from their Withdrawal Agreement rights).<sup>4</sup> The European Commission has accepted it has a role in ensuring EU member states fulfil these commitments for UK citizens living in the EU.

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\* The UK did lose its representation in EU institutions on 31 January 2019.

\*\* It also includes certain provisions to limit some of the cliff-edge changes that would otherwise arise from the UK leaving the transition period. For instance, Articles 40–46 of the Withdrawal Agreement allow goods placed on the UK or EU market before the end of transition to continue to their destination and be sold, avoiding potential disruption to goods in transit on 31 December. Other articles also provide for elements of policing and judicial co-operation to be wound down in an orderly way.

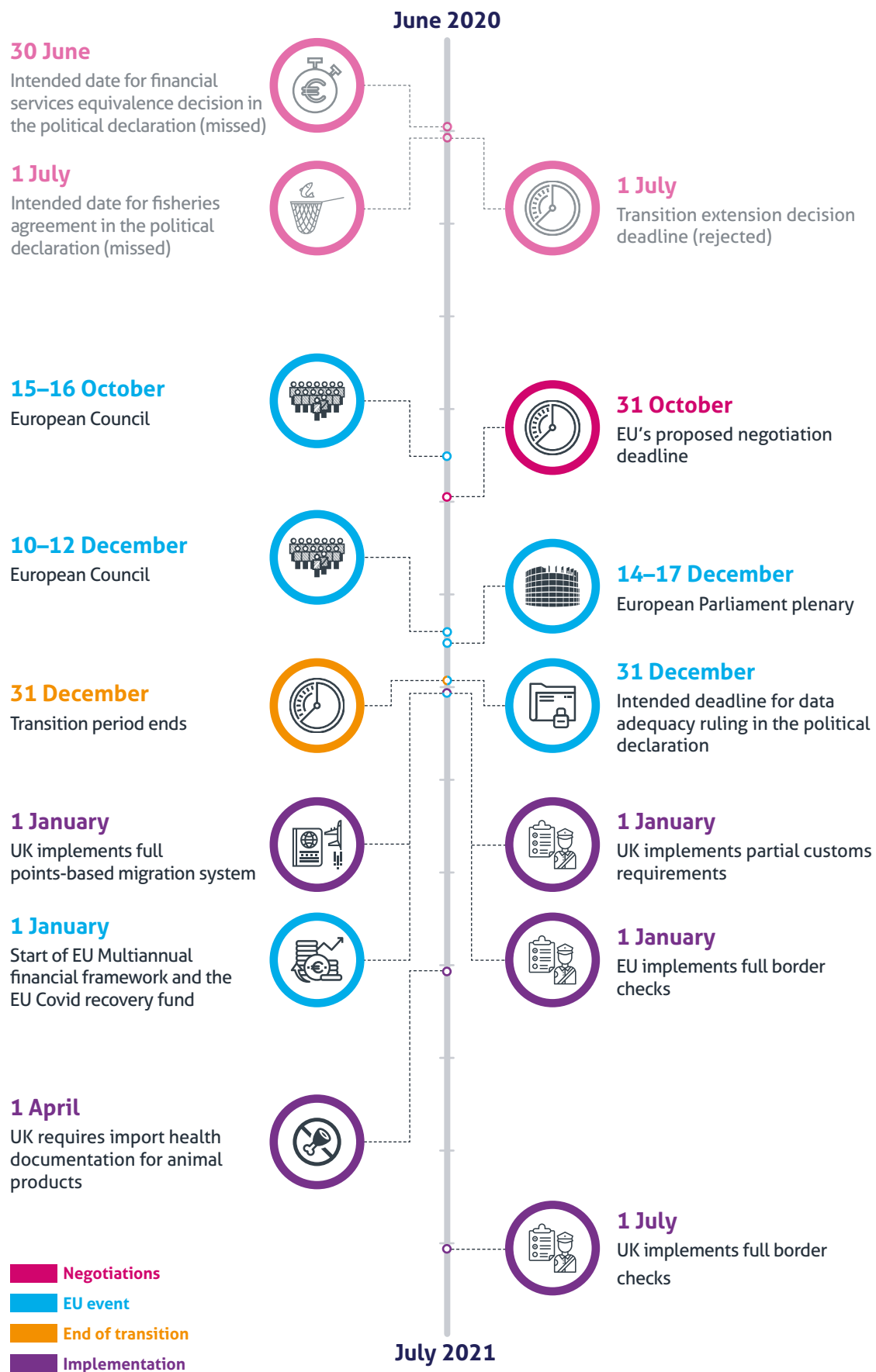
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The deadline for extending the transition period has now passed and the government has made clear that it has no intention of prolonging the status quo. That leaves less than six months for the UK and EU to prepare for a dramatically different trading relationship. As it stands, neither side is ready. In theory, it would be possible for the government to use other means to buy more time to negotiate or implement a deal, but as our recent [Institute for Government report](#) has highlighted, these are far from straightforward.<sup>5</sup>

This paper focuses on the actions business and government need to take before 31 December; the impact of coronavirus on these preparations; the extent to which uncertainty over the future relationship has impacted on businesses' ability to prepare for Brexit; as well as the key areas where more work is needed by both government and businesses.

A detailed assessment of the government's progress in implementing the Withdrawal Agreement, and in preparing for the changing security relationship, is beyond the scope of this report – as is a discussion of the actions individuals will need to take before the end of the year. But these changes remain important; and will be the subject of future Institute for Government work.

Figure 1 Key Brexit milestones, June 2020 – July 2021



Source: Institute for Government analysis.

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## Coronavirus has made it harder to prepare for Brexit

The urgency of the coronavirus response has taken resources and attention away from the government's Brexit preparations. For instance, HMRC is the department responsible for drawing up many of the new border processes that will be required from January 2021, but has had to invest its resources instead into implementing major parts of the government's economic response to the coronavirus crisis, including the Coronavirus Job Retention Scheme (CJRS, or 'furlough') and the Self-Employed Income Support Scheme.<sup>6</sup>

Other departments have also been affected; as of 9 June, half of Department for Transport (DfT) staff were working on the coronavirus response directly or indirectly, with the department responsible for ensuring transport routes remain operational and 'Covid-secure' during the pandemic.<sup>7</sup> The Department for Business, Energy and Industrial Strategy (BEIS) similarly reprioritised 160 staff from Brexit preparations. As of 17 June, only 38 of this number had returned to Brexit work.<sup>8</sup>

Similarly, civil servants who had been working on the 'Get Ready for Brexit' campaign last year were moved to work on coronavirus communications as the crisis developed in March 2020 (they have since returned).<sup>9</sup> Officials in the Department of Health and Social Care (DHSC) working on no deal were also redeployed to the coronavirus response – as was the no-deal lead in NHS England.

Businesses have also moved those working on Brexit – who often had project- and crisis-management skills – to work on their own coronavirus responses. Adam Marshall, the director general of the British Chambers of Commerce (BCC), said at a recent event that "attention has not been on Brexit in the last four months in most businesses, out of sheer necessity", explaining that the focus has been on keeping businesses afloat, dealing with cashflows, supporting employees and mitigating disruption to supply chains.<sup>10</sup>

Some firms furloughed staff in order to stay afloat, including some of those who had been responsible for Brexit preparations. The Freight Transport Association has said that three quarters of its members were using the government's furlough scheme in June, affecting its Brexit preparations.<sup>11</sup> Firms are now beginning to refocus on Brexit (and most industry groups have continued to work on the issues throughout the crisis), but two to three months of preparation time have been lost.<sup>12</sup>

### Businesses' Brexit preparations have gone backwards during the Covid-19 crisis

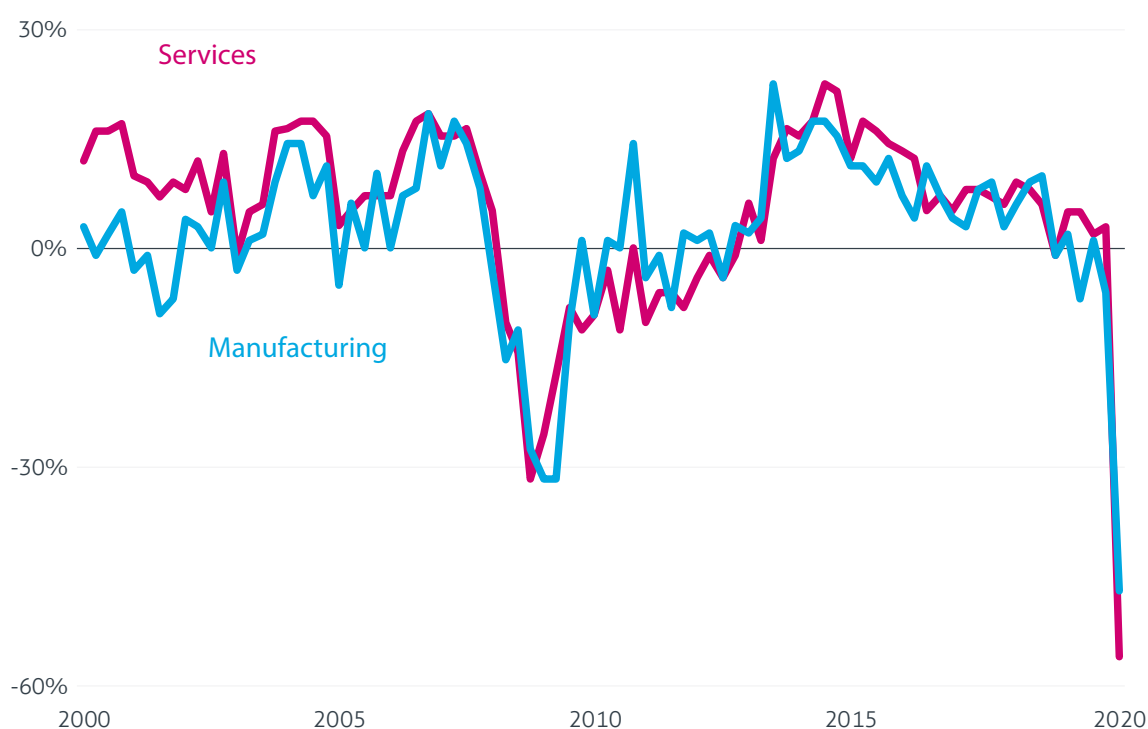
The coronavirus crisis has not only held up progress on Brexit preparations but, in some areas, has actually set businesses back, with the Confederation of British Industry (CBI) concluding: "preparations for the end of transition haven't just stalled, they've gone backwards".<sup>13</sup> Many businesses and public bodies have run down stockpiles built up ahead of a potential no-deal Brexit last year, either because it was not economically viable to maintain excess supplies or to mitigate the disruption caused by gaps and delays in supply chains caused by the coronavirus.<sup>14</sup>

Stockpiling will be hampered by a mix of limited warehouse capacity in the run-up to Christmas (when larger inventories are required), supply chains being strained by coronavirus disruption and costs proving prohibitive to businesses faced with a major hit to their cashflow due to the coronavirus (as shown in Figure 2). Some sectors – such as health and social care – are especially vulnerable. Supplies of medicines and medical devices built up on government advice last year have been partially depleted during the coronavirus crisis.<sup>15</sup> Rebuilding these will be difficult as there continues to be disruption to international supply chains,<sup>16</sup> while some countries have imposed bans on the export of some drugs.<sup>17</sup> The risk of a spike in demand in the event of a potential second wave of coronavirus makes rebuilding stockpiles all the more difficult.

For businesses trading in goods, preparing for Brexit means adapting supply chains to mitigate against possible disruption, responding to new regulatory barriers and guarding against the risk of new tariffs should a tariff-free free-trade agreement (FTA) not be reached. Yet the economic disruption wrought by the coronavirus crisis means it is hard to predict how supply chains will look in six months' time. Some sectors, such as motor manufacturing, are unsure about the extent of damage caused to their complex supply chains – which were among the first to bear the brunt of coronavirus disruption – and will not know for sure how resilient they have been until they begin scaling production up to more normal levels towards the end of the year.

New restrictions resulting from localised Covid-19 outbreaks also pose a risk of unpredictable and repeated disruptions to supply over the coming months – as already indicated by outbreaks in abattoirs and food manufacturing plants across Europe and the UK.<sup>18</sup>

Figure 2 **Percentage balance of firms reporting improved cashflow on the previous quarter**



Source: British Chambers of Commerce, *Quarterly Economic Survey* data, [www.britishchambers.org.uk/page/economic-data](http://www.britishchambers.org.uk/page/economic-data)



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The CBI has said that 80% of retailers and 62% of service firms have reported cashflow issues during the coronavirus crisis.<sup>19</sup> As a result, many firms have eaten into 'rainy day' cash reserves just to stay afloat – money that could otherwise have been used to prepare for Brexit. The BCC found that half of businesses reported that they had just three months or less in cash reserves.<sup>20</sup> The devastating impact of the virus on many firms' balance sheets means businesses are less likely to have the funds to invest in new systems, staff and training – even in areas where some government grants are available.<sup>21</sup>

The wider economic consequences of the coronavirus crisis also mean that businesses are preparing for Brexit against a much weaker economic outlook than last year.<sup>22</sup> Such uncertainty means it is difficult to predict what trading conditions will prevail at the end of 2020. Low economic growth both in the UK and globally will also mean it will be harder for businesses to replace any demand they lose from the EU with demand from elsewhere.

These problems are compounded by the fact that one of the government's main coronavirus economic support measures, the CJRS, will begin to taper away from August and is due to be wound down completely by 31 October. While the government has said it will pay employers a 'Job Retention Bonus' to keep previously furloughed employees on past October, this money will not hit firms' bank accounts until February. In short, the support withdrawn over the autumn could still lead to a wave of redundancies and insolvencies – just at the point when firms are bracing themselves for the impact of the Brexit changes.<sup>23</sup>

### **Weathering coronavirus does not mean businesses can handle Brexit**

Coronavirus and Brexit pose different problems for business. This means that the adaptations some businesses have made to manage disruption during the coronavirus crisis do not necessarily leave them better prepared for Brexit.

The food and drink sector is a prime example. Here, supply chains have largely held up during the coronavirus crisis, with imports from the EU largely uninterrupted and, in some cases, increasing.<sup>24</sup> However, the British Retail Consortium has warned that "if we get a disorderly Brexit, we potentially face a bigger challenge than the food supply chain faced in Covid", as supply *could* be interrupted by disruption at the border.<sup>25</sup> The UK imports around 40% of its vegetables and 37% of its fruit from the EU.<sup>26</sup>

For many of these (and other fresh produce), stockpiling is not an option, maintaining an uninterrupted supply essential to avoiding shortages on the shelves. The fact border changes will begin to come into effect in winter – when the UK is particularly reliant on imported produce – only exacerbates the potential problem.

Other sectors that have been worst hit by coronavirus, for example retail and hospitality, are less likely to be directly affected by a disorderly Brexit – though would suffer if food prices rise or supply is disrupted.<sup>27</sup>

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## Full preparation is impossible until the outcome of the Brexit negotiations is known

Four years on from the EU referendum, it is still not clear exactly what Brexit will look like. This makes it much harder for businesses to prepare.

First, they do not yet know whether there will be a deal. In some areas, the difference between an agreement and no-agreement outcome is small – for instance, customs and VAT, which will change irrespective of the outcome of negotiations. But the outcome could lead to large differences in other areas, such as agricultural tariffs.

Second, even if a deal is struck, businesses do not yet know what it will look like. The ambitions of the UK and EU differ greatly in areas such as trade in services and mutual recognition of standards. What needs to be done to prepare here, even in less high-profile areas, is dependent on the terms of any agreement.

Finally, business preparations are not just dependent on a deal (or lack thereof) – they rely also on unilateral decisions taken by the EU. These could mitigate disruption and limit what must be done before the end of the year. For example, in 2019 the EU legislated to allow UK lorry drivers to drive in the EU for a limited period even after a no-deal Brexit, without the need for additional permits.

### Businesses need to prepare to pay tariffs if no agreement is reached

Both the UK and EU [negotiating mandates](#) seek an FTA with zero tariffs or quotas.<sup>28</sup> However, if no (or a limited) agreement is reached, tariffs and full customs, as well as food and animal health checks, will be imposed on many goods moving between GB and the EU (and vice versa).

The introduction of tariffs would impose an additional financial burden on businesses trading between GB and the EU, requiring firms to be ready to calculate and pay tariffs on their goods. Although there would also be administrative costs even if the UK reaches a preferential trade agreement with the EU (more on this is discussed later). In some cases, firms may adjust their prices to pass the additional costs to customers, whether they be other businesses or the public.

The imposition of tariffs could even make some businesses unviable. For instance, some car manufacturers, typically operating on tight 2–4% profit margins<sup>29</sup> with supply chains embedded in the EU, may find it difficult to sustain their current UK manufacturing operations in a no-deal scenario, with Nissan warning in June that its Sunderland plant could become unviable if a tariff-free FTA cannot be agreed.<sup>30</sup> The EU's Most Favoured Nation (MFN) tariff\* of 10% on cars imported into the EU,<sup>31</sup> combined with possible disruption to supply chains, could make them uncompetitive in the long run. This is particularly true given there has been wider consolidation in the industry over recent years as firms seek to reduce costs and adapt to changing consumer demands.<sup>32</sup>

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\* Tariffs that a country or customs union applies to imports from all other World Trade Organization (WTO) members with which it does not have a trade agreement, in line with the WTO's MFN principle.

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Similarly, many UK sheep farmers have narrow profit margins and sell a high percentage of exports into the EU; seven of the top 10 importers of UK lamb are in the EU.<sup>33</sup> Sheep farmers could find it difficult to remain competitive if there is no agreement between the UK and EU,<sup>34</sup> as tariffs equivalent to around 90% would then be imposed on some cuts of lamb.<sup>35</sup>

Tariffs will affect those importing into the UK, too. The additional costs may mean that importers need to find alternative sources of supply. Businesses' ability to find alternative cost-effective suppliers will depend in part on which of the EU's existing trade agreements the UK has managed to roll over before the end of the transition period, and any new FTAs the government negotiates. As of 29 June, only 20 out of 38 such deals had been agreed.<sup>36</sup>

For businesses most vulnerable to the impact of tariffs, preparing for an outcome which does not provide zero-tariff and zero-quota access between the UK and EU markets may mean preparing to fundamentally restructure, scale down production or close completely. Few firms are willing to set such potentially drastic plans in motion until the outcome of negotiations is clearer.

### **A deal would mean businesses have to be ready to comply with rules of origin**

To benefit from an FTA, businesses would have to comply with [Rules of Origin](#) (RoO). These are complex, but in simple terms they define how much of a good can come from countries outside a free trade area before it ceases to benefit from the preferential terms of the relevant FTA.<sup>37</sup> For example, under the EU–Canada trade agreement (the Comprehensive Economic and Trade Agreement, or CETA), a car will not qualify for preferential tariffs if more than 50% of the value of its parts comes from outside the EU and/or Canada; these percentages are known as content thresholds.\* Businesses in both countries have to be able to prove that their goods contain sufficient 'originating content'.

This would be a sizeable and expensive administrative burden for UK firms with complex European supply chains that have not previously had to trace the origin of their goods (bearing in mind that some goods are made up of many thousands of components). The administrative and compliance costs associated with RoO could amount to anywhere between 4% and 15% of the cost of goods sold – so some businesses may choose not to take advantage of the preferential treatment afforded by the FTA and pay MFN tariffs instead.<sup>38</sup>

Some businesses may ultimately need to reshape their supply chains to comply with RoO in a UK–EU FTA, buying more of their components from the UK and EU and less from third countries. But it will be difficult for them to know whether they need to do so until content thresholds are agreed in any UK–EU deal. While past EU FTAs may provide some guidance of the sorts of rules that may apply, the precise terms often vary by agreement. The situation is made more difficult by the fact that neither the UK nor EU has published a draft set of RoO during negotiations.

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\* For some goods and under some agreements, these conditions can be much stricter. For example, a sausage will not qualify for preferential treatment under CETA unless the meat in it comes from animals that were born, reared and slaughtered in the EU or Canada. Under the US–Canada–Mexico trade agreement, at least 66% of a car's content has to come from one of the parties, rising to 75% after four years.

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But this should not stop businesses that export goods from beginning to prepare their documentation on where their inputs are sourced from. Under any UK–EU deal, businesses would need to prove their compliance with RoO – even if they are well over whatever threshold turns out to be required. Even if no agreement is reached with the EU, UK firms that currently trade with countries such as South Korea under EU FTAs that are being ‘rolled over’ will need to make sure that they still comply with the revised RoO, given that components of EU origin will no longer qualify as ‘originating’ from the UK for the purposes of a UK–South Korea FTA.

The government, too, would need to make additional preparations if RoO are to apply. For example, HMRC would need to provide advice and advance rulings to businesses on the origin of goods, which would require additional resources.

### **In other areas, an agreement could reduce burdens – but not eliminate them**

A deal could mean other preparations are not needed. Mutual recognition agreements between the UK and EU would, for example, reduce the need for businesses to seek approval from two sets of regulators or have their goods retested in a new laboratory.

It could also reduce the processes at the border. Some easements could be negotiated through standalone agreements, even if an FTA is not reached. For instance, the UK and EU could agree to reduce the percentage of animal product exports subject to physical inspection: the EU–New Zealand sanitary agreement limits checks on some animal products to 1–2%.<sup>39</sup> However, regardless of any FTA, EU rules require that live animals imported into the EU are physically inspected.<sup>40</sup>

Both sides could also agree to mutual recognition of each other’s ‘trusted trader’ schemes, easing border formalities for authorised firms that frequently transport goods across the border. They could also agree to waive or streamline safety and security declarations, reducing the number of forms that businesses need to complete – although not removing the need altogether. Taken together, these measures could have the potential to reduce both the readiness burden for businesses and the time taken to cross the border.

For firms and individuals trading services with the EU, the UK government’s draft legal text proposes a broad interpretation of permitted activity under the EU’s short-term visitor arrangements. This would allow certain service providers to visit the EU for short stays without work permits. If this is not agreed, service providers would need to be prepared to comply with each member state’s restrictions on what activity is, or is not, permitted on short-term visits – any providers not covered by an agreement would have to do this in any case. Whatever happens, UK citizens will be subject to the rule that they can only spend 90 out of any 180 days in the Schengen area.<sup>41</sup>

The UK is also asking for an agreement on the mutual recognition of professional qualifications that goes beyond what is typically found in FTAs,<sup>42</sup> with the UK mandate proposing an FTA should “provide a pathway for the mutual recognition of professional qualifications”.<sup>43</sup> If the EU were to agree to these proposals, it would ease the burden

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on companies and individuals trading services with the EU – although these proposals do not offer the same benefits as staying in the single market, and are not directly enforceable by individuals in the courts. At this stage in the negotiations, the EU has rejected both of these proposals as unacceptable “cherry-picking”.

### **The UK will also be reliant on decisions the EU will make unilaterally**

Some critical decisions are not up for negotiation – for these, the UK is waiting on unilateral EU decisions. One is on data: whether the EU deems the UK data regulatory regime ‘adequate’ will have significant implications for how data can be transferred between the EU and UK and types of preparations that will need to be taken.<sup>44</sup>

If the UK’s data regime is deemed adequate, UK firms will only need to continue to comply with UK data regulations and will be able to continue transferring data between the EU and UK as they do now. If not, firms will have to fall back on more cumbersome alternatives – such as Standard Contractual Clauses (SCCs), which require written agreement between companies sharing DATA.\* The recent *Schrems II* case in the European Court of Justice sets a high bar for their use, requiring that they provide protection essentially equivalent to that guaranteed within the EU by the General Data Protection Regulation (GDPR).<sup>45</sup>

Many large businesses, particularly in the services sector, took steps to prepare for a lack of a data adequacy decision in the run-up to a potential no deal last year by drafting SCCs to include in contracts. The UK Information Commissioner’s Office also provided draft clauses for businesses to use.<sup>46</sup> Aviva – a UK-based multinational insurance firm – said that as of 26 February 2020, 85% of its contracts had been amended to include SCCs.<sup>47</sup> Other firms put in place binding corporate rules, which allow entities within the same organisation to share data freely across the EU border. But smaller companies are less likely to have prepared.

The European Commission plans to make a decision on data adequacy by 31 December 2020.<sup>48</sup> If the it does not grant the UK data adequacy and businesses are not prepared, there is a real risk that data flows between the EU and UK will be heavily disrupted and that many businesses will find themselves non-compliant with data protection regulations, risking infringement proceedings and fines.

The EU is also set to decide whether to grant the UK ‘equivalence’ in financial services.\*\* This would involve the EU recognising the UK’s regulatory regime for financial services, making it easier for some parts of the financial services sector to trade between the UK and EU from the end of the transition period – particularly investment banking and insurance.<sup>49</sup> In theory this decision can be revoked with 30 days’ notice, so the UK has asked for a more structured process around withdrawal.

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\* A lack of data adequacy could also make it more difficult for UK police and security services to share information relevant to criminal investigations – for example criminal records and DNA (although this would also depend on reaching an agreement on internal security co-operation). See our recent report [Negotiating Brexit: Preparing for talks on the UK’s future relationship with the EU](#) for more details.

\*\* There is no single ‘equivalence’ decision. Equivalence can be granted across 12 different EU Directives and Regulations covering a range of financial and related services.

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The initial deadline to reach a decision by 30 June has been missed and recent comments by Michel Barnier, chief negotiator for the EU, has criticised a delayed response to the EU's equivalent-assessment questionnaires.<sup>50</sup> The UK has blamed the EU for delays.<sup>51</sup> If the EU does not grant equivalence, banks in the UK would have to operate with poorer market access (although equivalence itself would provide a narrower market access for UK firms than passporting<sup>\*</sup>).<sup>52</sup>

### **The services sector is better prepared for the end of transition**

The direction of negotiations – with a commitment to leave the single market – means that many parts of the services sector have known for a long time that there will be a significant change in their trading relationship with the EU from the end of the transition period.

For highly regulated sectors, such as legal and financial services, regulators have also compelled businesses to prepare.<sup>53</sup> Steps taken ahead of a possible no deal in 2019 can be carried over for the end of the transition period. For example, professional, legal and financial service firms have already taken measures to comply with different rules of establishment according to member states' rules – such as restructuring their businesses, re-writing articles of association, establishing new subsidiaries in the EU and moving some operations to existing EU offices. In some instances, firms have complied, or will need to comply, with requirements for a certain proportion of a subsidiary's board or ownership to be held by member state nationals or residents.<sup>54</sup> Firms have also had to apply for the relevant licences and permissions from the relevant regulating body in the member state in which they are operating.

Other parts of the sector have also made their preparations. Commercial broadcasters operating in the EU using a UK license will need to apply for a license in an EU member state to continue operating beyond the end of the transition period. This process takes up to three months and may require broadcasters to establish offices in the EU and make changes to their operations to comply with their new regulator's rules.<sup>55</sup> Most of the approximately 600 firms<sup>56</sup> affected took steps to re-register ahead of last year's Brexit deadlines.

As UK professional qualifications may not be recognised in the EU after the end of the transition period, some firms have taken steps to re-qualify staff in the EU; for example some lawyers have re-qualified to practise in the Republic of Ireland<sup>57</sup> so they can continue to offer advice in the EU and retain rights of audience in EU courts. Compared to the risk of no deal last March and October, the Withdrawal Agreement does mean that EU citizens resident in the UK (and UK citizens in the EU) before the end of the transition period will have their professional qualifications recognised beyond December 2020.<sup>58</sup> But these arrangements do not cover UK citizens residing in the UK and traveling to the EU to work – or vice versa.

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\* Within the single market, financial services can be provided from the UK into the EU with a single authorisation or 'passport' issued by that UK authorities, and vice versa.

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Although many services firms are largely prepared, there is more to be done. For example not all current business has migrated over to the new operating models – which could still take some time.<sup>59</sup> Some EU member states could change, or update, their rules, for example on the provision of legal services, which firms would need to be ready to adjust to. As with other sectors, smaller firms also tend to be less prepared than larger ones.

## **The government's own preparations have been delayed**

Until the coronavirus crisis, Brexit had been the government's main priority since the EU referendum. Thousands of civil servants have been working to unpick the UK and EU relationship and prepare for new UK regulatory regimes, design new UK systems and databases and pass necessary legislation – in particular the EU (Withdrawal) Act 2018 – to address any legal gaps which would arise from leaving the EU.\* Where changes have been inevitable, it has been easier to prepare, for example building up the capabilities in certain public bodies that will take over responsibilities from EU institutions. But even four years is an extremely short timeline for such a huge task.

During the Article 50 period, the Department for Exiting the EU (DExEU) co-ordinated preparations across government and was responsible for ensuring no-deal preparations were in place ahead of March and October 2019 – although relevant parts of DExEU reported to Michael Gove, as chancellor of the Duchy of Lancaster, under Boris Johnson. Since the department was dissolved, this responsibility has moved to the Cabinet Office, with Gove continuing to have overall responsibility for the government's Brexit preparations. Within the Cabinet Office, the recently renamed Border and Protocol Delivery Group is responsible for co-ordinating across government departments and agencies on preparations for the border.

Some of the preparations made ahead of the possible no deal in 2019 have laid the foundation for the work undertaken this year. For example, the Department for Environment, Food and Rural Affairs (Defra) developed the UK Import of Products, Animals, Food and Feed System (IPAFFS) to replace the equivalent EU system for notifying UK authorities about the import of animal and plant products (although the government had some concerns about how it would function in the event of no deal in March last year).<sup>60</sup> HMRC has had to prepare the Customs Handling of Import and Export Freight (CHIEF) system – for recording the movement of goods – to be ready to cope with five times the number of annual customs declarations.<sup>61</sup>

But last year the UK intended to waive most checks in the immediate aftermath of a no-deal Brexit, prioritising 'flow' and introducing Transitional Simplified Procedures to facilitate this.<sup>62</sup> Although some systems had been designed and the capability of others improved, significant disruption at the border on day one was anticipated.<sup>63</sup> This risk has not gone away.

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\* Further primary legislation still needs to be passed to implement post-transition domestic policy regimes in areas such as agriculture, fisheries, trade and immigration. Progress on these bills has been delayed by the coronavirus crisis.

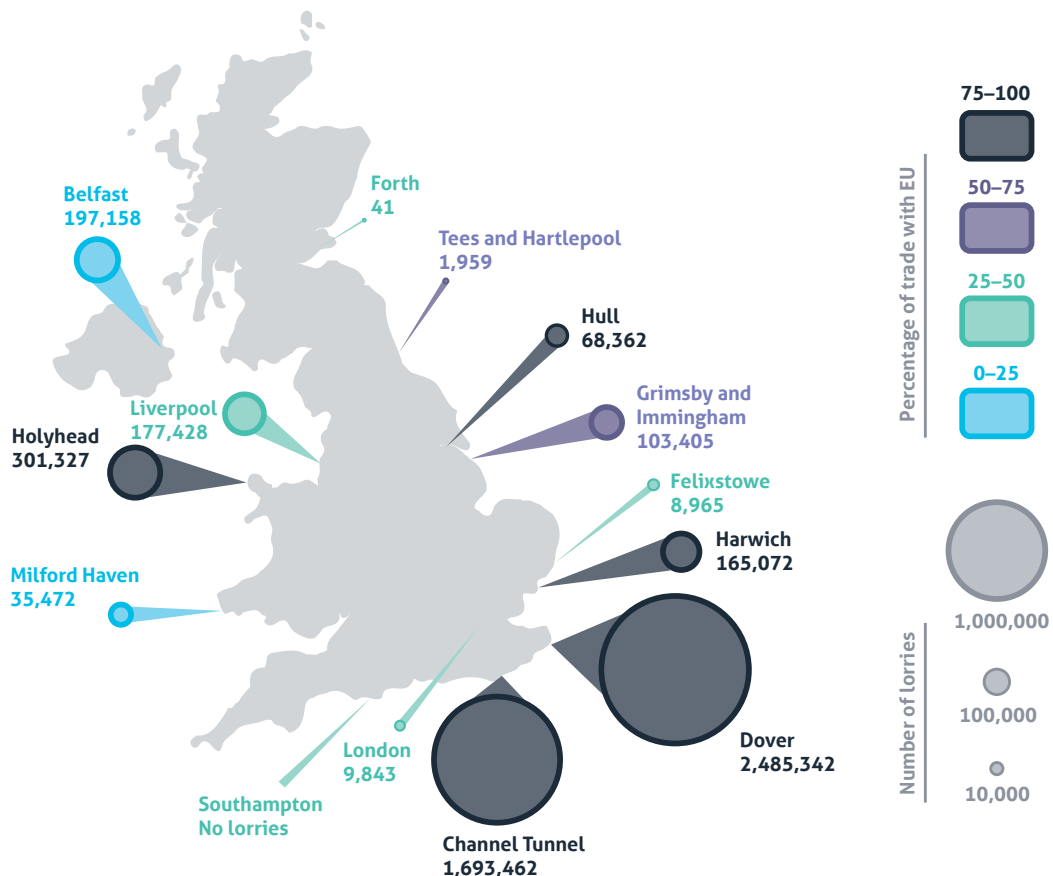
## The UK border is not ready for Brexit

Leaving the single market and customs union will fundamentally change the way the GB–EU border operates (the Northern Ireland protocol provides separate arrangements for the GB–NI and NI–Republic of Ireland borders). Moving goods across the English Channel will require businesses to comply with new checks, including customs checks, sanitary and phytosanitary (SPS) checks, and safety and security checks.<sup>64</sup>

In theory, businesses have been able to take some steps to prepare for new border formalities, for example by appointing customs intermediaries to complete customs formalities on their behalf – although the low numbers of trained customs agents has hindered this. Businesses have also, if they do not already have them, been able to apply for HMRC accounts needed to complete customs processes,<sup>65</sup> calculate the customs value of their goods and work out which commodity codes apply to their goods.<sup>66</sup>

But those operating and using the border also need to know how the new requirements will be administered in practice, such as what forms must be completed and when, what IT systems will be used and where physical checks will take place. Clarity about how the border will work at the short straits Channel crossings between Dover/Folkestone and Calais/Dunkirk is particularly important. As Figure 3 shows, the straits play a vital role in UK–EU trade and much of this trade is 'Roll-on Roll-off' (RoRo) – where goods stay on the back of a lorry and are driven onto a ferry or trains transiting the Channel Tunnel.

Figure 3 **Annual lorry traffic and EU share of trade for selected major UK ports in 2018**



Source: Institute for Government analysis of Department for Transport, Maritime and Shipping Statistics.



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The process on the French side of the border has been clear for some time. Last year, the desire to protect the integrity of the single market meant that, unlike the UK, the EU was planning on applying full checks in a no-deal scenario. It also has well-established rules for third countries under the Union Customs Code. A new border operating model was introduced by French authorities in Calais and Dunkirk and underwent live trials before October 2019.<sup>67</sup> Traders planning to transit through these ports from the end of the transition period can already make the necessary preparations – for instance, by ensuring they are registered with the appropriate systems and familiar with the paperwork required.

The UK had no existing customs processes suitable for the RoRo traffic arriving in Dover and Folkestone, and so has had to develop a new framework from scratch. The government was originally due to share the initial drafts of its new 'Border Operating Model' (BOM) with industry in March,<sup>68</sup> with three rounds of consultation planned between then and September. However, partial proposals were only shared with industry in June<sup>69</sup> and a revised version was only made public on 13 July.<sup>70</sup>

The publication of a detailed BOM is welcome, but much needs to be done to be ready for the end of the year. There are still some gaps still to be filled in: after all, it is one thing knowing that customs forms are needed, but quite another knowing what needs to be written on them.

Greater clarity over the UK side of the border will be particularly welcomed by freight forwarders and customs intermediaries, who will bear the brunt of responsibility for complying with new requirements. Port operators – such as the Port of Dover and Eurotunnel – also need to understand the details of how the new border will work, as they are often responsible for collecting much of the necessary information on behalf of government authorities. The Port of Dover has said it is "too early to tell" whether six months is long enough to phase in new border processes.<sup>71</sup>

The published BOM indicates that the government also needs to roll out an entirely new IT system – the Goods Vehicle Movements Service (GVMS) – to allow traders to pre-lodge relevant paperwork and give vehicles the right approvals before crossing the border. GVMS will also need to process goods moving from Great Britain to Northern Ireland, and needs to be ready for such goods by January<sup>72</sup> – although will only be used for transit movement of goods<sup>\*</sup> being imported into GB in January. The BOM indicates that the government plans to make GVMS available for the rest of EU trade in July 2021 (where border locations have chosen to introduce it).<sup>73</sup>

GVMS is yet to be finalised and will not be tested until November.<sup>74</sup> That may seem dangerously close to the December deadline, however it is worth noting that the French equivalent model, SI Brexit, was designed and tested to a similar timeframe ahead of the potential no deal in October last year.<sup>75</sup> Although some in industry have suggested that the UK would be better served by licensing the French system, instead of building a bespoke system in just a few months.<sup>76</sup>

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\* This is for goods being moved under the Common Transit Convention, which avoids customs checks at each border a good crosses, allowing customs checks to be completed away from the border.

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## Delaying new checks is no magic bullet

To ease the introduction of customs formalities, the UK government plans to phase in customs requirements for imports from the EU over a six-month period.<sup>77</sup> This phased approach means that only 'light touch' customs declarations will be required from January, with traders able to defer detailed declarations and payment of duties for six months. Full safety and security declarations as well as full SPS (animal and plant health) checks will only be required from July 2021.<sup>78,\*</sup>

The delay reflects the government's recognition that businesses face huge pressures dealing with coronavirus and Brexit simultaneously,<sup>79</sup> but is also a signal that the government itself is not ready. In February, Michael Gove announced that full checks would be implemented from the end of the year.<sup>80</sup> Even before coronavirus, this timeline looked very ambitious.

The phased introduction of UK customs formalities has been broadly welcomed by businesses – providing more time to prepare and easing cashflow pressures in the first half of 2021. However, it does not remove the readiness challenges. Since Gove's announcement in February, some (predominantly large) firms have already started preparing for the introduction of full customs formalities from the end of the transition period. Some of these businesses would rather submit full declarations from January 2021, rather than having to delay until July.<sup>81</sup>

There is also a risk that the phased implementation could serve merely to delay the disruption caused by poor preparedness from 1 January 2021 to 1 July 2021. The international trade secretary, Liz Truss, has also expressed concern that the phased approach could fall foul of WTO MFN rules (although most experts have argued there is unlikely to be any real fallout from this)<sup>82</sup> and may provide opportunities for smuggling.<sup>83</sup>

The government has also not announced whether it will re-introduce the Transitional Simplified Procedures (TSP) it introduced last year as part of its no-deal planning. TSP allowed traders to access the simplified customs measures. It was relatively easy to apply for, and the government ended up auto-enrolling VAT-registered businesses anyway.<sup>84</sup> This time, traders will have to access these simplifications using pre-existing standard simplified declarations procedures, which require more administrative work from businesses – including proving a good record of customs compliance.<sup>85</sup> This will be difficult for those who have only traded (freely) with the EU before.

What the phased approach has done is buy the government more time to set up the physical infrastructure necessary to support new systems and accommodate full physical checks. The government has recently announced £705 million of funding for new infrastructure, jobs and technology at the GB–EU border.<sup>86</sup>

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\* From January 2021, physical checks at the point of destination or other approved premises will apply for all high-risk live animals and plants, and standard customs declarations will apply to controlled goods like alcohol. From April 2021, all products of animal origin and all regulated plants and plant products will also require pre-notification and the relevant health documentation.

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However, with space constraints at Dover and Folkestone, most new infrastructure will need to be located away from the border itself – the government recently confirmed it was looking at five sites in Kent where it intends to build new infrastructure,<sup>87</sup> and has purchased a 27-acre site near Ashford, 22 miles inland from Dover.<sup>88</sup>

The EU has ruled out reciprocating the UK's phased approach; traders will need to be ready for full customs checks on the EU side of the border from 1 January.<sup>89</sup> The different UK and EU approaches will also complicate the message as to what businesses need to be ready for and when they need to be ready. Given the high volume of traffic using the short Channel straits (with over 400 commercial vessels per day)<sup>90</sup> and the time-sensitive nature of RoRo shipping, a lack of preparedness for EU checks could lead to delays on both sides of the border.<sup>91</sup>

This means the government may still need to revisit last year's no-deal plans, reviving Operation Brock to check hauliers have the correct paperwork before they reach the Channel ports at places like Manston Airport and other sites in Kent, as well as to manage the flow of traffic in Kent in case of border disruption.<sup>92</sup> In the BOM, the government has announced a new Smart Freight Service system to help ensure RoRo freight traffic have the correct paperwork, although acknowledges it could potentially form part of a revived Operation Brock.<sup>93</sup>

These proposed easements will also not apply to the GB–NI border as the UK is required by the Withdrawal Agreement to ensure the Northern Ireland protocol is fully operational by 1 January 2021. If no agreement on the future relationship is reached, there will be additional requirements placed on goods moving between the two. In particular, if there is no agreement on a zero-tariff FTA, the UK will be required to apply the EU tariff to any goods deemed 'at risk' of subsequently moving into the EU.

### **There are currently not enough new customs agents to handle new border formalities**

Even as the UK border process becomes clearer, the UK currently lacks the customs agents necessary to process up to 215 million additional customs declarations each year.<sup>94</sup> In February, the government indicated that around 50,000 additional private sector customs agents would be needed to meet demand.<sup>95</sup> But industry leaders have suggested the true figure is likely to be smaller (around 35,000)<sup>96</sup> and even lower if an agreement on zero tariffs is reached, since customs formalities would be easier to complete.<sup>97</sup>

The government has provided £84m of funding to support the training of additional customs agents, and has worked to help establish a 'customs academy', which provides training, alongside various other private sector offerings.<sup>98</sup>

However, far fewer customs agents than are needed have been trained so far, even when judged against the lower-end estimates,<sup>99</sup> and it is unclear if existing operators have the capability, or appetite, to expand capacity. There is also the question of whether enough people would be willing or able to train and/or relocate to become customs agents in time.

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Firms are reluctant to train new staff and take on new salary costs to provide capacity that may not be needed in full for 12 months. Logistics specialists have also warned of a focus on expanding existing operators rather than providing opportunities for new entrants.<sup>100</sup> There are also concerns that classroom-based customs training cannot replace real-world experience, which can take around a year to gain.<sup>101</sup>

Some customs intermediaries have prioritised supporting their existing clients as they scale up, which may make it difficult for the 180,000 'new' traders<sup>102</sup> – those expected to make customs declarations for the first time – whose exports go only to the EU and who are therefore unlikely to have existing customs relationships.

The government has also announced £10m to recruit an additional 500 UK Border Force staff to handle additional checks at the border.<sup>103</sup>

### **The UK's new immigration system is not yet up and running**

The government has committed to ending freedom of movement by the end of the year. The immigration system will then treat non-resident EU and European Economic Area (EEA) nationals\* as the same as those from the rest of the world – meaning they will require visas to live and work in the UK.

The Home Office set out further detail on the new rules on 13 July, including more information on how the new points-based immigration system will work. It also confirms a new health and care visa, which will be a fast-track process with reduced fees for doctors, nurses and other 'skilled' healthcare staff, but notably not for social care workers, and restoration of the post-study work route for non-EU students graduating from UK universities.<sup>104</sup>

However, the Immigration and Social Security Bill, which sets out the framework for the new system, has not yet been passed. Some specifics, such as the list of shortage occupations (jobs where there are not enough resident workers to meet demand and that will benefit from preferential treatment), have not yet been made public as they have been subject to consultation.<sup>105</sup> As a result, some policy decisions have yet to be taken and full guidance on how the system will work has not yet been provided. More detail is forthcoming, but with questions so fundamental to UK employers' staffing requirements still to be answered, the government is leaving precious little time for businesses to adapt for the changes in January.

Preparing for the new system poses a major challenge for business and the Home Office. At present, only those firms recruiting from outside the EU, EEA or Switzerland need to register with the Home Office as visa sponsors. Around 30,000 such firms are registered.<sup>106</sup>

As with other preparations, there is significant variation between sectors and businesses in their ability to prepare. For larger businesses and parts of the public sector, such as NHS trusts, the task is one of upscaling and modifying existing systems to cope with EU migrants. This is because they are more accustomed to recruiting from outside the EU, so have systems in place to handle work visa applications and associated bureaucracy. From January, the process for recruiting from, say, France will

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\* This will not apply to Irish citizens who are part of the Common Travel Area.

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be the same as from Nigeria. Some sectors that are less reliant on EU labour, such as manufacturing and technology, may hope to benefit from a more liberal rest-of-the-world (non-EU) migration regime.

For the approximately 340,000 small and medium enterprises (SMEs)<sup>107</sup> which currently employ EEA nationals but have little or no experience of recruiting from the rest of the world, the preparation task is greater. The social care, food manufacturing and hospitality sectors are particularly exposed. The logistics sector is also reliant on EU labour, employing EU nationals as 13% of its staff, with a declining share of UK nationals over time.<sup>108</sup>

If firms in these sectors wish to continue recruiting from the EU beyond the end of the transition period, they will need to register as a visor sponsor with the Home Office – a process that is costly, and that can take up to three or four months and may be further impacted by administrative difficulties caused by coronavirus.

When taking a typical notice period of three months into account, this means any UK firms hoping to employ EU nationals from January will likely need to start making job offers from late September – and applying to be a visa sponsor sooner than that. Cash-strapped businesses that hope to continue recruiting from the EU will also need to absorb the heavy costs involved in sponsoring visas.<sup>109</sup>

The Home Office, and specifically its UK Visas and Immigration (UKVI) division, will need sufficient capacity to deal with new sponsor applications and field queries from those unaccustomed with immigration procedures. From January, the department will then need to process a far greater number of visas, too – estimated at potentially double what it currently handles.<sup>110</sup>

This is no small task – and comes at a time when the Home Office is also working on improving the online tool used by businesses, developing new immigration systems such as the EU Settled Status Scheme, and working to uphold its commitment to implement the recommendations of the Windrush review.<sup>111</sup> Preparing for a new immigration system in six months, alongside these other commitments, will be a strain on resources.

## **The readiness task is far from complete**

Despite some positive steps, particularly since the June transition deadline has passed, there is still a lot government and businesses need to do. To drive readiness in industry, the government now must provide clarity about what needs to be done and when – and communicate this effectively with the public.

### **An effective communications campaign will be crucial**

In the run-up to the 31 October 2019 deadline, the government ran a controversial 'Get Ready for Brexit' campaign, aimed at raising awareness and pointing business and individuals to material on GOV.UK. The government has recently launched a similar campaign for the end of the transition period with the title 'The UK's new start: let's get going'.

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The campaign includes a new 'Check, Change, Go' strapline that will be used across TV, radio and online advertisements in the run-up to December, as well as direct channels such as text messages and webinars.<sup>112</sup> With the Institute of Directors reporting that only a quarter of business leaders say their organisations are fully ready,<sup>113</sup> this campaign will be an essential part of driving preparedness. But lessons also need to be learned from last year.

As the National Audit Office (NAO) acknowledged in January, the Get Ready for Brexit communications campaign was a complex task. It needed to reach multiple audiences – from sophisticated and well-resourced multinational companies to sole traders – and required cross-government co-ordination.<sup>114</sup> This proved difficult even when Brexit was the government's key priority, not least because the exceptional politics surrounding the Benn Act in the autumn of 2019 made the no-deal Brexit the campaign was aimed at preparing the public for look unlikely.<sup>115</sup>

This time around, the government will have to work hard to convince a Brexit-weary and distracted public that this time is different – with the added complication of communicating coronavirus guidelines at the same time. As the government has acknowledged, being clear that either outcome – agreement or no agreement – will involve large-scale changes must be a priority.<sup>116</sup>

But many businesses and industry groups also believe the previous campaign was poorly pitched: it focused on headline messages and provided little detail on exactly what businesses and individuals actually needed to do. On customs, for example, one of the campaign's key message was to encourage businesses to apply for a 'GB EORI number'<sup>117</sup> – despite the fact that these had already been automatically assigned to some 88,000 VAT-registered businesses a month earlier (although, many non-VAT registered businesses still needed to secure a number).<sup>118</sup>

To communicate effectively, the government must strike the balance between providing detailed information and ensuring accessibility.

This year, the government has improved its Brexit landing page by adding video and providing better signposting to the actions users need to take. The website also links to an updated 'checker tool' that allows users to more easily find information relevant to their specific circumstances and sign up for email alerts when the advice they need to follow is updated. Attention is also paid to performance analytics and user feedback when updating the material offered.<sup>119</sup> This is an improvement on the campaign run ahead of a possible no-deal Brexit in March 2019, when detailed technical notices were provided that were difficult for SMEs that lacked access to expert resources to digest. However, care still needs to be taken to ensure that guidance for the end of the transition period is accessible.

Industry groups have also called on the government to 'think like business' and provide information in a way that addresses the practical questions firms have about what they need to do.<sup>120</sup> This may involve providing information about both UK and EU requirements. For instance, a step-by-step and end-to-end explanation of how customs formalities will work on both sides of the border would be more useful to traders than information about UK preparations alone.

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Knowing who to target will also be important. The experience of the 2019 campaign should make the government better placed this time, having gained a better understanding of who needs to be reached.<sup>121</sup> Industry groups and key private sector organisations with important customer bases – like the Channel ports – will also play a key role in explaining new requirements to the public and disseminating information from the government. Reaching small businesses on both sides of the channel, which are generally ill-prepared for Brexit – will be vital.

But in other ways, preparing the public for Brexit will be harder this time around. The government will need to run coronavirus and Brexit campaigns side by side. This could put huge pressure on staff across Whitehall. The Public Accounts Committee (PAC) has highlighted that the Cabinet Office – responsible for both campaigns – may be particularly affected.<sup>122</sup> HMRC, and the business, health and social care and transport departments – likely to make the largest contributions to the new Brexit campaign – will be similarly stretched. Senior civil servants have told the PAC they believe the government can run both campaigns concurrently, though have already admitted it will be tough.<sup>123</sup>

Coronavirus itself – and the measures used against its spread – also create practical barriers to delivering an effective campaign. The former chief executive of the civil service, John Manzoni, told the PAC in March that communication campaigns need to raise awareness, build understanding and promote action.<sup>124</sup> He pointed to the success of the ‘ground campaign’ of roadshows, face-to-face meetings and pop-up events in significantly improving business readiness in 2019. In 2020 this is not so easy. The government plans to use a similar ‘field force’ team to provide one-to-one support to businesses and their supply chains this year<sup>125</sup> – but with gatherings restricted and social-distancing measures likely to persist for the foreseeable future, such events may need to be held virtually or – as the government has indicated – over the phone.

The government has said that additional information will be required to drive preparations for the Northern Ireland protocol – with further details expected in July. Given the uncertainty and complexity involved in the protocol, a lack of clarity about what businesses need to do to prepare remains a significant gap.

### **The government may need to give business more support – and time – to prepare**

Beyond providing information to the public, the government may need to take additional steps to drive readiness. One option would be to provide courses on new requirements and processes, particularly in areas where changes are highly technical – such as at the border and changes in regulatory regimes. Alternatively, the government could follow the Dutch model and provide businesses with funding or vouchers to hire consultants to explain how Brexit will impact their business and help them prepare.<sup>126</sup>

In 2019, the UK government made £8m available for firms to train customs agents – but there was little awareness and low take-up of the offer;<sup>127</sup> it also announced £10m to support trade associations and business groups to help businesses get ready.<sup>128</sup> It could repeat such offers.

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In some sectors, the government has provided money to help businesses to prepare – such as the £84m in funding to help train customs intermediaries, discussed earlier.<sup>129</sup> However, this may still not be enough – and concern about a lack of capacity in the sector may push the government to provide more support and allow funding to be used for a wider variety of preparations.

In the run-up to a possible no deal in March and October last year, the UK government intended to unilaterally recognise EU approvals in several areas. This was aimed at reducing the administrative burden placed on businesses and providing more time for them to adapt to new requirements and absorb the additional costs involved in seeking dual approval of products in the UK and EU and introducing new labelling. For instance, the UK planned to provide a grace period of between 4 and 12 months for medical devices already approved in the EU to comply with the new UK registration process.<sup>130</sup> Similarly, the UK Medical and Health Regulatory Authority planned to allow pharmaceutical companies a 33-month period to amend some packaging details for goods already on the market.<sup>131</sup>

The UK also planned to unilaterally recognise the 'CE' products standards mark in the event of a no deal Brexit last year, before requiring products to comply with the new UKCA standard.<sup>132</sup> The government could choose to apply this measure at the end of the transition period. The government has already said that some EU professional qualifications – including some legal qualifications – will continue to be recognised for a limited period beyond the end of the transition period, in order to allow individuals time to re-qualify in the UK.<sup>133</sup> The government should make it clear now which unilateral measures it will put in place to give businesses clarity about what they need to be prepared for on 1 January 2021.

In the run-up to the October deadline last year, the EU did not plan to reciprocate easements in most areas, but it did take some steps that covered basic arrangements for flights, financial services and road hauliers. This year, the EU has stuck firmly to the line that mitigations will not come from their end. The UK can only ease the readiness burden so much on its own.

Both sides may be reluctant to communicate frankly about Brexit or announce additional mitigations while negotiations are ongoing, for fear of showing their hand too early. But such brinkmanship would be a mistake – especially in areas where changes will happen regardless of the outcome of negotiations and it is in the interests of both sides that business is prepared.



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## Brexit will not be 'done' on 31 December 2020

### There will inevitably be disruption in January

Ahead of a possible no deal last year, the government was preparing for three scenarios: no deal; the UK's continued membership of the single market and customs union through an Article 50 extension (where it would also remain part of the EU); or exit under a ratified Withdrawal Agreement including a 'standstill transition period' until 31 December 2020. This meant that while the government prepared for the significant disruption of a potential no-deal exit in October, reaching agreement in 2019 meant that very little changed in practice in January 2020. Ahead of January 2021 this will not be the case – and huge changes will occur, whatever the outcome of negotiations.

Leaving the single market and customs union overnight will always entail a cliff edge – even if the government and businesses are fully prepared. In February 2020, in a speech at Université libre de Bruxelles, the UK's chief Brexit negotiator, David Frost, painted this as a "one-off cost" that was the acceptable price for greater freedom from Brussels.<sup>134</sup> But this does not reflect reality, and the end of transition does not entail just a one-off cost.

Some Brexit preparations, such as investing in new customs systems or setting up subsidiaries in the EU, do present one-off investments (even if potentially large ones). But additional bureaucracy combined with the higher costs involved in hiring from outside of the UK once free movement ends mean more expensive operations for UK businesses in the long term. These costs will be ongoing. Should no agreement be reached, companies will also be required to pay tariffs, also on an ongoing basis. Combined, these changes mean it will be slower, more costly and more difficult to do business with the EU than the status quo allows – and far from being a one-off cost to shoulder, this will be the case for the foreseeable future.

### The consequences of leaving the EU will last well beyond day one

When preparing for no deal in 2019, the government anticipated significant short-term disruption. A sub-set of its no-deal planning, Operation Yellowhammer, led out of the Civil Contingencies Secretariat, focused on planning for the 'reasonable worst-case scenario'.<sup>135</sup> It was this work that predicted reduced flow to 40–60% across the Channel straits, as well as a decrease in the availability and choice of fresh food in the UK.<sup>136</sup>

The end of the transition period does not pose exactly the same challenges as no deal did in 2019. The policy question of how to manage the border on the island of Ireland has been resolved – although inviting a huge operational task in doing so. But in many other areas, the possible disruption of 2019 and 2021 will be identical – whether or not a deal is agreed. Delays at the border could cause significant knock-on effects for 'just-in-time' supply chains, potentially precipitating widespread economic disruption while also turning parts of Kent into a lorry park. To manage this risk, the government will likely need to prepare to stand back up much of its Yellowhammer preparations, including 24-hour operational centres.

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Most of the government's no-deal preparations last year focused on what would happen in the days and weeks, rather than months, following a no-deal exit. In part, this reflects the fact that there was an expectation that no deal in 2019 would not necessarily rule out more negotiations further down the line – even if the EU insisted on the withdrawal issues being resolved first. Whether or not an agreement is reached at the end of the year, the government will need to be prepared to support businesses as they adjust to the new trading relationship, well beyond January 2021.

As no agreement at the end of this year would be due to an inability for the two sides to reach an acceptable compromise on the UK and EU future relationship, it could make it more politically uncomfortable for the UK to return to the negotiating table, although any economic fallout may shift the calculation. But even if the two side were to reopen talks, the risk remains that the no-agreement default would persist for some time – if not indefinitely.

### **The future relationship is unlikely to be fully resolved by December**

The UK's relationship with the EU may adapt over time. Certain negotiations may well continue beyond December 2020, not least on foreign policy, defence and security co-operation, which so far the UK government has refused to discuss.<sup>137</sup>

Even if a limited FTA is negotiated by the end of October, the EU's preferred deadline, negotiations on other sectors may continue beyond the end of the year – with unilateral measures plugging any gaps in the meantime.

If an agreement on certain areas cannot be reached, the EU and UK may choose to put in place certain mitigations that were planned in the event of no deal in 2019, for example on aviation and road haulage. The EU stated in March 2019 that UK aeroplanes could continue to fly and make some stops, and UK road freight could deliver a range of goods, in the EU (including mail and medicines) subject to the UK reciprocating measures.<sup>138</sup> These would either be superseded by an agreement or would fall away after a period of time, allowing both sides to adapt.

New Year's Eve 2020 may be the symbolic moment that the UK leaves the EU single market and customs union, but it will not be as final as many may think. The details of the trading relationship between the UK and EU could still be subject to discussion for many months into 2021, or beyond.

### **Brexit will have a long-term and uncertain impact on businesses and the UK economy**

It has been suggested that one of the reasons the government ruled out an extension to the transition period was to allow the economic impact of Brexit to be "masked" by the disruption wrought by the coronavirus crisis.<sup>139</sup> Whether or not this is fair, the already difficult task of assessing the exact impact of the UK severing ties with its closest and largest trading partner has been made much harder.

Businesses will need to adapt their operating models. In a no-agreement scenario this will mean calculating and paying new tariffs. Even if an agreement is reached, changes

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will be needed to assess and adjust to new non-tariff barriers to trade. Deciding how to do this will include decisions about whether to invest in the UK; where to locate supply chains; how to address new regulatory barriers; and whether it will be possible to pass on additional costs to consumers. Even if some firms are relatively well prepared for the start of the new trading realities in January, this does not guarantee longer-term viability: if it proves more costly to do business in the UK in the long term, some may change or wind down their operations in the UK.

The government will need to consider what level of support it may want to give certain businesses and sectors who face new barriers to trade – and what policies will be appropriate to a shifting economy. Operation Kingfisher, the government’s planning for economic intervention ahead of no deal in March and October 2019, will likely need to be revisited. This time around, any support for businesses affected by Brexit will also need to take account of the extensive economic interventions made in response to the coronavirus pandemic, as of July 2020 totalling an arresting £188bn of crisis spending.<sup>140</sup> Future uncertainty over the possibility of a second wave of the virus hitting the UK in autumn will also have an impact on the decisions the government will face.

It may be that leaving the EU presents opportunities for some businesses – particularly those which primarily trade with the rest of the world, rather than the EU. That said, any UK businesses trading with those ‘third countries’ under the terms of FTAs currently enjoyed through the UK’s EU membership that *aren’t* successfully rolled over (Canada, for example) will face additional barriers. As the government looks to strike new trade deals with other countries, it will need to consider how UK industry can take advantage of those opportunities. With trade negotiations with multiple countries ongoing, uncertainty over trading conditions will remain for some time.

## Conclusion

Preparing for Brexit was always going to be a huge task, and it is clear that there is still much to do. The coronavirus crisis has only made things more difficult, undermining some existing preparations, delaying others, and making it harder to prepare for the end of the year.

In some areas, progress has been made. The UK government is largely better prepared than last year, but that is not true for all businesses.

Ongoing uncertainty about the outcome of negotiations and the lack of detail about the UK and EU’s post-Brexit policies mean that businesses and individuals still do not know exactly what it is they are preparing for. And, as in 2019, many businesses – particularly small and medium sized enterprises – are reluctant to begin complex preparatory work until what is expected of them is clearer.

Some are unwilling to spend money on preparations that may prove unnecessary. Here, many feel they have been burnt before, having seen funds wasted in their preparation for the no-deal ‘near-misses’ of 2019. Others are simply unaware that changes in trading

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conditions will occur, or how they will affect them. Worryingly, UK government data suggests that as of June 2020, more than half (61%) of British businesses have made no preparations at all for leaving the EU.<sup>141</sup>

With less than six months to go, providing certainty to business must be a priority for the government. It needs to work with business to establish what support will be needed to adjust to the changes at the end of the year. Crucially, this should be factored into any economic response to the coronavirus crisis.

The government also needs to decide exactly which of the mitigations it was prepared to introduce last year ahead of a potential no deal it will put in place this year – and clearly communicate that to business. Businesses need to understand what scenario they should be planning for – while the ongoing negotiations in some cases make this difficult, there is more certainty government can give.

Finally, any communications campaign needs to build on clear, signposted information about what steps business needs to take – and when. The government should learn the lessons of the flawed 'Get Ready for Brexit' campaign and present information in a way that reflects how business operates on the ground.

In rejecting an extension to the transition period, the government has set itself a monumental task. With time running out it must now begin fighting on two fronts: keeping the public safe while also preparing it for 31 December – and beyond.

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