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# Brexit Industry Insights

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## Energy

With the UK's default to leave the EU without a deal, the energy sector is not immune to the impact of Brexit. The sector is faced with simultaneously navigating longer term transformation in how energy is produced and consumed, an increasing focus on decarbonisation and decentralisation, whilst mitigating the impacts of Brexit in the short term. The risk of the UK leaving the EU without a deal remains high, and the time to act is now.

### Brexit and the Energy Sector

The energy sector is diverse, and the impact of Brexit will vary for different players in the industry depending on market focus, the energy products traded and the cost base. Many oil and gas companies established in the UK have global operations and are already well-versed at navigating a diverse political and regulatory landscape. Brexit is another change to this landscape that companies will need to manage. The UK's withdrawal from the EU will see the UK leave the EU's internal energy market. In 2017 the energy sector created £83.7bn in economic activity and supported 682,000 jobs[1]. The UK is a net importer of electricity and gas; in 2017, the UK imported 4.2% of its electricity demand through interconnectors, and 36.8% of its gas[2].

### What does this mean for business?

Some of the key implications for businesses operating in the sector are:

**Cross-border supply chains**

In a no-deal scenario, movements of goods between the UK and the EU27 would become imports and exports, resulting in customs compliance obligations. The EU applies a zero rate of duty to most hydrocarbon products for non-EU members. Post-Brexit, the UK's draft no-deal tariff indicates it would take a similar approach to duty rates. Chemicals, plastics and equipment are more likely to be subject to a duty cost, which could impact energy supply chains, e.g. for energy infrastructure and spare parts.
Border delays could arise in a no deal Brexit, impacting the resilience of supply chains, especially in relation to critical spare parts or inputs to the refining process.

International commercial terms (INCOTERMS) will indicate which party is contractually responsible for customs duties and formalities. Trading businesses will often place responsibility for acting as importer or exporter of record – and completing the relevant customs clearance requirements – on a local counterparty. There is an increasing focus on INCOTERMS used as a result of Brexit and other changes in the international trading environment, in particular trade tensions between the US and China.

1. https://www.energy-uk.org.uk/energy-industry/energy-in-the-uk.html
2. Commons Library Paper CBP8394, 'Brexit: Energy and Climate Change'

### Tax

Many trading companies rely on EU VAT simplifications, such as triangulation. When the UK leaves the EU, these EU simplifications will no longer apply to UK VAT registrations, which could lead to additional VAT registrations and associated administrative requirements, e.g. some EU member states require non-EU established entities to appoint a fiscal representative.

EU Directives, including the Parent-Subsidiary and Interest and Royalties Directives, will no longer apply. Accordingly relief from foreign withholding taxes arising in EU member states will rely on the application of double tax treaties. For multinational extractive companies, the wider tax landscape in both the UK and overseas is increasingly an item on the board agenda, irrespective of the Brexit outcome.

### Regulation and legal

There will be a number of regulatory changes which companies will need to manage, for example:

**Derivatives trading**
Financial services is a highly regulated sector and trading in commodity derivatives contracts may constitute a regulated activity. In a no-deal Brexit scenario, the UK will be outside of the EU's framework for financial services regulation. The UK has implemented temporary transition provisions for EU businesses, but where UK companies trade on EU exchanges or trade with EU counterparties, EU regulatory requirements will need to be met.

**Chemical substances**
In the absence of a regulatory alignment between the UK and EU, UK-based firms subject to the EU's Registration, Evaluation, Authorisation & restriction of Chemicals (REACH) will face a regulatory trade barrier as their REACH registrations become invalid in a no-deal Brexit. In order to continue doing business in the EU post-Brexit, UK businesses will need to appoint an only representative or transfer registrations to an EU entity (although transfer of licenses could be a complex process as specific rules apply)[3].

**Export controls on dual-use items (items which can be used for both civil and military purposes, such as chemicals)**
The overall framework of controls will not change, but there will be new licence requirements. Licences will be required for exports from the UK to the EU and vice versa, and an export licence issued by one of the 27 EU countries will no longer be valid for export from the UK.

**Contractual clauses may need updating to manage some of the potential risks arising from Brexit or in response to Brexit-related restructuring. Areas of focus include**
reviewing risk allocation between parties such as which counterparty bears the risk of border delays and tariff costs; definitions of key terms; changes to pricing structure or frequency of pricing reviews and changes to payment terms and contract enforcement.

### In focus: climate change and Brexit

The UK will remain party to the United Nations Framework Convention on Climate Change (UNFCCC) and Kyoto Protocol, as part of international efforts to combat climate change. The UK's Climate Change Act establishes more ambitious emissions reduction targets than those set by the EU, requiring the UK to bring all greenhouse gas emissions to net zero by 2050. Brexit is not expected to impact the UK's domestic strategy, but the nature of the UK's relationships with both the EU and the rest of the world remains unclear.

The EU Emissions Trading Scheme (ETS) is an international greenhouse gas emission trading scheme. Installations in the UK will no longer be subject to the EU ETS in a no-deal scenario. In order to ensure smooth operation of the EU ETS, the European Commission adopted contingency measures including the suspension of processes in the UK from 1 January 2019. The UK government will not issue any 2019 allowances unless and until the suspension is lifted.

The UK government's 2018 Budget detailed that in a no-deal scenario the UK government would introduce a Carbon Emissions Tax (CET) on carbon dioxide (and other greenhouse gases on a carbon equivalent basis) from UK stationary installations currently in the EU ETS. Provisions for a CET are included in Finance Act 2019. Over the longer term, the UK government is seeking agreement with the EU for a linked UK ETS, and is exploring carbon pricing options.

3. European Chemicals Agency, EU exit: https://echa.europa.eu/uk-withdrawal-from-the-eu
4. Trading electricity if there's no Brexit deal: https://www.gov.uk/government/publications/trading-electricity-if-theres-no-brexit-deal/trading-electricity-if-theres-no-brexit-deal

Many issues outlined above will apply to utility companies and those trading gas and power. In addition, the EU's Regulation on Energy Market Integrity and Transparency (REMIT) prohibits insider trading and energy market manipulation and makes provision for monitoring of the market by regulators. UK market participants trading in the EU will need to register with an EU regulatory authority to avoid a disruption to cross-border trade, trade within EU wholesale energy markets, or trade within the Single Electricity Market. It is expected the UK will maintain the majority of REMIT in a no-deal scenario.

Some UK-based energy trading firms are either setting up trading desks in the EU, with requisite regulatory authorisations, or building on existing EU operations. Those operating in the nuclear sector will need to be prepared for new licensing requirements on dual use goods and changes to the authorisations for spent fuel and radioactive waste[6].

### Utilities and trading gas and electricity with the EU

In a no-deal Brexit, EU energy laws will no longer apply in the UK. Alternative arrangements are in place for trading of electricity via interconnectors in the event of a no-deal scenario[4], although trading on interconnectors will be less efficient. The mechanisms of cross-border trading of gas are not expected to fundamentally change[5], although there will be changes to access rule approval, operator certification and gas network codes.

Post-Brexit, the UK will no longer be a member of Euratom and has passed legislation so the Office for Nuclear Regulation oversees domestic safeguards, and signed new agreements with the International Atomic Energy Agency (IAEA) to replace the existing trilateral agreements between the IAEA, Euratom and the UK.

### People

Under a no deal, free movement of people will end once the UK leaves the EU. EU/EEA citizens resident in the UK before 31 October 2019 will retain their rights to settlement and access to services, and they will need to apply under the EU settlement scheme by 31 December 2020. EU/EEA citizens moving to the UK after 31 October 2019 will for a transitional period be able to move to the UK to live and work as they do now. But those wishing to stay beyond December 2020 will either need to apply for European Temporary Leave to Remain by 31 December 2020 or leave the UK. The UK is expected to introduce a new immigration regime from January 2021 for all EU nationals arriving in the UK after this date.

Multinational energy companies often have a highly mobile international workforce and are reliant on the efficient deployment of individuals around the world including within the EU. Post-Brexit changes will need to be factored into existing processes to avoid delays in putting feet on the ground and/or increased costs. For example, immigration requirements for UK nationals planning to work in the EU will need to be confirmed on a country-by-country basis including expected time lines for completion of the immigration process.

Dual social security liabilities could arise for employers and mobile employees if member states do not agree to reciprocal arrangements with the UK.

## What can businesses do to prepare?

- Continue to monitor key sources of information including:
  - Government advice from the UK government (Department for Business, Energy and Industrial Strategy, Ofgem and the Department for Exiting the European Union), the EU, and other countries in which your business operates in.
  - Trade associations and industry bodies, including Energy UK.
- Continue to engage with and encourage your existing workforce to certify their residency status while also reviewing recruitment strategy for critical roles. Concurrently, monitor information from countries in which you operate to ensure you understand local visa and work permit requirements.
- Make sure you know how to complete and submit the necessary customs declaration procedures and forms for imports and exports. Register for an Economic Operators Registration and Identification (EORI) number and assess INCOTERMS for who bears the impact of losing beneficial trade terms.
- Undertake a regulatory review to understand what the changes to REACH could mean for your products where they are produced and sold.
- Perform a legal review to identify potential contractual risks as a result of Brexit. Identify impacted terms and plan response, e.g. the creation of a precedent bank of terms for future re-negotiation, immediate re-negotiation or re-papering.
- Ramp up your operational response capability and take steps to manage disruption as and when it occurs, including accelerating imports/shipments, identifying warehousing space as well as alternative suppliers and/ or markets.

5. Trading gas with the EU if there's no Brexit deal: https://www.gov.uk/government/publications/trading-gas-with-the-eu-if-theres-no-brexit-deal/trading-gas-with-the-eu-if-theres-no-brexit-deal
6. Nuclear sector summary guidance: https://www.gov.uk/guidance/the-nuclear-sector-and-preparing-for-eu-exit

### Energy supplies in Ireland

The UK government is continuing to work with the Irish government and the European Commission to seek agreement that the Single Electricity Market on the island of Ireland will continue. Ireland will have no direct connection to the main EU energy infrastructure post-Brexit. The Irish Offshore Operators Association (IOOA) estimated the potential cost of a total blackout in Ireland for a day would be £850m[7].

International and EU regulations require countries to hold emergency oil stocks. Under EU rules, these stocks can be held anywhere in the EU. Approximately one third of Ireland's emergency oil stocks are held in the UK[8]. The Irish government has indicated that as a result of Brexit, it will move these stocks to Ireland and other EU member states. This is likely to mean some stocks are held further away from Ireland, leading to additional transport time and costs.

- Manage all key stakeholders to understand commitments and expectations. Engage with audit committees and liaise with trade bodies and regulators on preparations.

7. Irish Offshore Operators Association: Value of Indigenous Oil and Gas Industry to ireland https://www.iooa.ie/wp-content/uploads/2019/01/IOOA_report_web.pdf
8. Irish Offshore Operators Association: as above

## How can Deloitte help?

Deloitte has been supporting multiple businesses across a range of industries to understand the implications of, and prepare for, the UK's withdrawal from the EU. We have supported many clients with their Brexit planning. Our teams combine Brexit insights, industry knowledge and technical expertise to support our clients with their Brexit readiness planning – from risk assessment to applying the lessons learned to optimise for the future trading environment.

For further information please contact Deloitte Brexit Support at **brexitsupport@deloitte.co.uk**

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### Further reading

**Official no-deal guidance for the energy sector**

**UK No-deal Technical Notices:**
Trading electricity if there's no Brexit deal
Trading gas with the EU if there's no Brexit deal
Civil nuclear regulation if there's no Brexit deal
Generating low-carbon electricity if there's no Brexit deal
Nuclear research if there's no Brexit deal
Running an oil or gas business if there's no Brexit deal

**UK Business Preparation Tool:**
Prepare your business or organisation for Brexit

**European Commission Brexit Preparedness:**
EURATOM
Internal Energy Market
Guarantees of the origin of electricity from renewable energy sources

**Ofgem**
Preparing for EU exit

This no-deal guidance is not exhaustive. Companies should routinely review the latest official updates and technical guidance as and when they are published by the UK, EU, and individual EU Member States.



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