WHITE & CASE

Brexit: Rebalancing your European workforce

Whatever form Brexit takes, international companies with operations in the UK are planning ahead to retain access to the EU market

Brexit: Rebalancing your European workforce

Considering relocating your business after Brexit? The decision on whether to move employees outside the UK is not a straightforward one and requires careful assessment, say **Nicholas Greenacre** and **Sarah Taylor** of global law firm White & Case.

Britain's exit from the EU is still unfolding and the exact terms that will affect employers and employees based in the UK are unknown. Nonetheless, international companies with offices in the UK are looking ahead for strategies to relocate their employees to other member states in order to retain the business advantages of EU policies.

It may take months, if not years, before we know the answer to key questions about how Brexit will be implemented. For example, how British companies will access European markets and the status of Britain's immigrant workers may not be known for some time. However, what is certain now is that businesses are thinking about the consequences of Brexit and the next steps that will need to be taken for them to continue to operate within the EU.

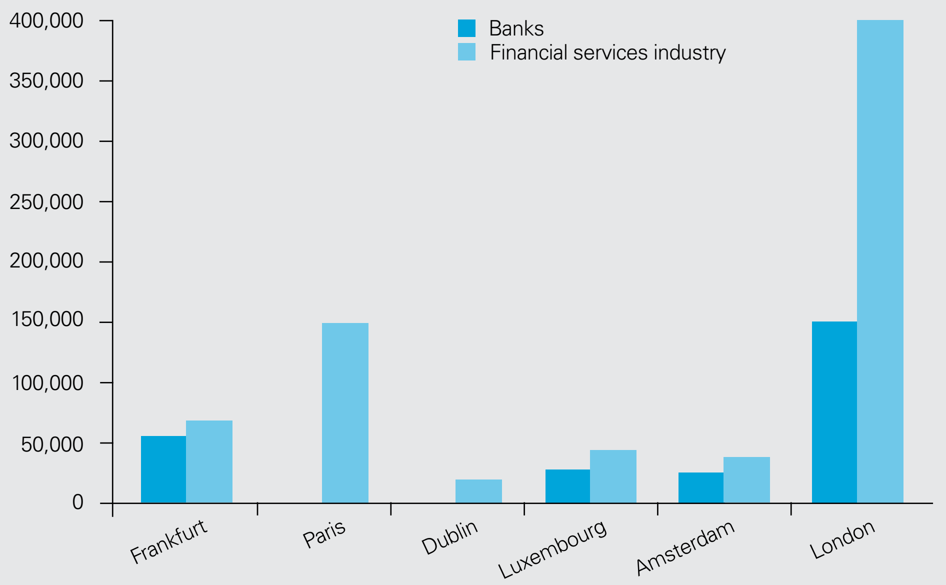
According to reports, HSBC and Goldman Sachs are among the financial services institutions that have already indicated that they may move staff outside the UK and virtually every other international group with a UK platform is likely to have this issue on its agenda.

The decision on whether to move employees outside the UK is a complex one and the shape that Brexit will take is just one of the factors that need to be considered. The attitude of UK-based staff to a move overseas and the availability of suitably skilled employees in the chosen location, income tax and social security rates, employment laws, and accessibility to suppliers, customers and advisers are just some of the points that influence the decision of where a business and its employees should be located.

Brexit notwithstanding, London and the UK will retain some key advantages—particularly in the financial services sector, one of its strongest industries. As Dr. Martin Lück, chief investment strategist at

Comparison of financial services sector in Europe

Number of employees in 2015



Sources: Federal Employment Agency, Deutsche Bundesbank, INSEE, ONS, Stationery Office, Statec, Helaba Research

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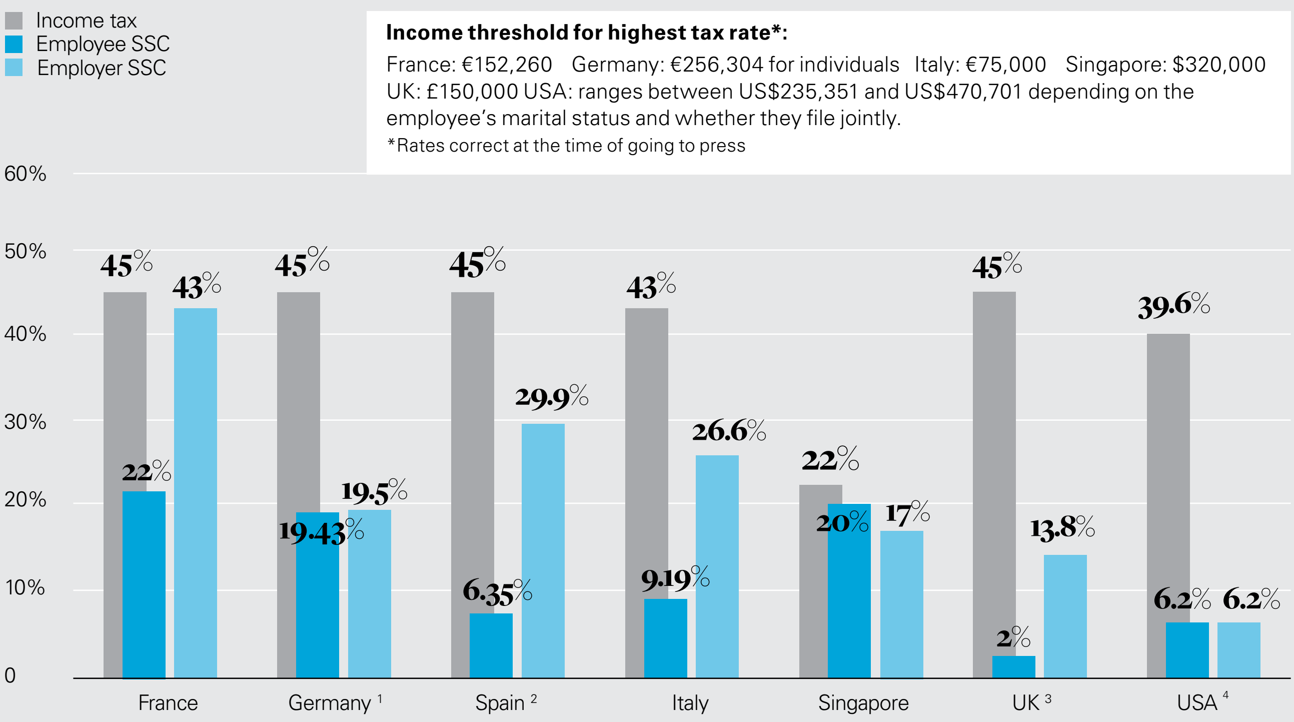
Comparison of highest marginal rates of income tax and social security contributions (SSC)



[1] Salary capped at income ceiling for social security in state pension insurance: Western states: €6,350 per month; Eastern states: €5,700 per month
[2] Income tax in Spain may vary depending on the autonomous region where the employee works
[3] Rate shown is based on an employee earning above the upper earning limit
[4] Highest federal income tax rate is shown and social security contributions are exclusive of other employment-related taxes,

Source: White & Case

Blackrock—the world's biggest fund manager—said recently, "I do not think that London will lose its status as the financial hub in Europe, simply because this status has evolved over decades, if not centuries. I think it will broadly remain the same."

Language of global business

London has significant advantages for businesses ranging from the primacy of English as the global business language to its position between American and Asian time zones. Over the years, the city has built up infrastructure that serves highly remunerated, internationally mobile people very well, and has schools, shops and restaurants of every international variety. The UK financial services regulatory regime

£2.2bn

Investment by foreign companies into the UK's financial companies in 2015

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is viewed as one of the most robust among developed financial markets, and English law is used to arbitrate most international trade disputes. These factors have helped the City of London become one of the most global financial centres. According to TheCityUK, foreign companies invested more than £2.2 billion into the UK's financial services institutions in 2015, while the 2.2 million employees in financial services across the country—two-thirds of them in London—dwarf that of rival centres like Frankfurt and Paris. The other large financial centres in Europe are upping their game when it comes to attracting the business that the City could lose as a result of Britain's decision to leave the EU, and rival locations are launching

At a glance: Employment rules in key geographies

	No significant issues	Some issues to consider but not barriers	Significant issues that may make operations impractical or impossible
Recruitment	Germany, Ireland, Italy, UK, US, Singapore	France, Spain	
Termination of employment	US, Singapore	Ireland, Italy, Spain, UK	France, Germany
Consultation with employee representative bodies	Ireland, UK, US, Singapore	Germany, Italy, Spain, France	
Restrictions on variable pay for bankers	US, Singapore	France, Germany, Ireland, Italy, Spain, UK	
Special tax treatment for inpatriates	France, Italy		

Source: White & Case

campaigns to attract businesses dissatisfied by Brexit. German government officials have been visiting London-based US investment banks to advertise Frankfurt's attractions, while Paris has been running an advertising campaign urging businesses to 'swap the fog for the frogs'. In January 2017, HSBC announced the transfer of 1,000 investment banking positions to Paris as a consequence of Brexit.

Most recently, Citigroup has chosen Frankfurt as the post-Brexit hub for its European investment banking business. This decision is likely to see around 200 London-based jobs move to the German city before Britain leaves the EU in 2019. Citigroup's decision will bolster Frankfurt's position as the city most likely to benefit from London's investment banking migration after Brexit.

France and Italy have added financial sweeteners by proposing tax incentives for returning nationals. A special tax regime applies to employees who are transferred by a foreign or non-French company to work at an affiliated company in France or hired outside of France directly by a French company, become French tax residents upon taking up their new position in France, and have not been tax resident in France in the five years before the year they take up their new position in France. The regime provides employees and executives with a French income tax exemption of 30 per cent of their total net remuneration linked to inpatriation to France and for all remuneration that relates to an activity performed outside the country. This favourable tax treatment lasts for up to eight years.

The Italian authorities have recently released official guidelines on the new regime for people who are newly tax resident in the country. The special regime allows a 50 per cent reduction of taxable employment and self-employment income earned by

Location, location, location—shifting the focus

Since the UK voted to leave the EU in June 2016, details have emerged about the plans of businesses and financial institutions considering shifting certain operations to other European cities. So far, these have included the relocation of employees based in the UK to other European offices, extending operational activities and opening new offices in other European cities.

	Luxembourg	Ireland	Germany	Netherlands	Belgium	France
3i	■					
AIG	■					
Bank of America	■	■				
Barclays		■				
Blackstone	■					
Carlyle	■					
Citigroup		■	■	■		
Credit Suisse		■		■	■	
Deutsche Bank			■	■		
EQT Partners	■					
Goldman Sachs	■	■	■			
HSBC						■
Intermediate Capital Group	■					
JP Morgan	■	■	■			
Lloyds of London					■	
Morgan Stanley	■	■	■			
Standard Chartered			■			
UBS			■			

Source: Adapted from KPMG, *Brexit strategy implementation,* Recent relocations announcements, June 2017

individuals who are relocating to Italy and meet specific requirements, for example, those who qualified as an Italian non-tax resident for at least five years prior to their transfer to Italy and then maintain Italian tax residency for at least two years.

The big move

But the decision on whether or not to relocate is based on more than these incentives. Companies are taking account of the fiscal, employment and regulatory regimes in other countries before deciding whether to move some, or all, of their operations. Assessing the impact of all these variables is challenging. Reforming employment laws will play a key part in attracting businesses to move away from

> **Europe is not the only alternative post-Brexit location: North America and Asia can look like attractive destinations**

50%
Tax reduction for individuals who are relocating to Italy and meet specific requirements

London to rival locations. It would seem, however, that the grass is not always greener. It has been widely reported that companies are reluctant to move jobs to Paris following Britain's exit from the EU due to France's protectionist labour laws which see work councils playing a key role in relations between employee and employer. Generous employee protection regulations can also encourage companies to be more circumspect about offering permanent jobs. According to research by Eurofund, more than one in 10 employees across the EU is on a temporary contract and, in France,it is estimated that four out of five new hires are on short-term contracts.

Bankers have cast doubt on the chances of France luring much of the

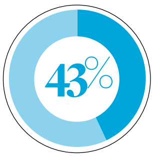
UK's financial industry after the Brexit vote, and cite the country's unstable tax regime and labour rules that make employees difficult to fire as major deterrents. An employee who is unfairly dismissed can challenge his or her dismissal before the employment tribunal and, if the dismissal is found to be unfair, the courts can grant compensation. Compensation is usually financial, but in some limited cases, the employee has a right to be reinstated in his or her previous position. Indeed, the French government has recognised this issue. While successive French presidents have, over the years, tried to ease restrictions imposed on businesses, they have had little success. After a consultation with the national unions and other social partners in May and June 2017, the new incumbent, Emmanuel Macron, communicated on 30 August 2017 five draft legislative orders which aim to amend materially France's labour laws. This legislative reform will provide companies with much more flexibility to manage their headcount in France and guarantee them stability and security, notably in the case of collective dismissals (by imposing caps and a fixed scale of damages for unfair dismissal). This reform should help Paris attract businesses away from London. President Macron recently published the five legislative orders and aims to implement them progressively during the coming months. The French government has also unveiled plans to scrap the bonuses of traders and banking executives classified by the European Banking Authority as 'risk takers' from the calculation of severance pay, with a view to making redundancies in France less expensive to the employer. This reform is likely to take effect by the end of 2017.

And what of other major European countries? Italy has set up a task force to lure businesses and investors from London to Milan in the wake of Brexit, with the Italian government aggressively promoting Italy's financial capital as a viable alternative to London.

Milan is home to Italy's main stock exchange, has two airports and boasts Bocconi University, one of Europe's most acclaimed for business studies and finance. The city's profile was boosted last year by the success of the Expo world fair, which attracted 20 million visitors. But Milan faces numerous obstacles, from language to labour laws. Italy has one of the lowest levels of English language proficiency of any country in the EU according to a study by the European Commission—and firms looking to leave the UK might instead opt for Dublin over Milan. High social security costs also mean that employees in Milan are more costly than those in London and rigid labour laws make it harder to dismiss employees. Furthermore, Italy's legal system is notoriously slow and inefficient, with court cases dragging on for years and even decades. Companies may have concerns about the extra costs to set up a business in Milan.

Despite being subject to EU law, the UK has a more flexible labour system than France or Germany.

In Germany, the threshold for justifying termination of employment is quite high and, as a result, other proportionate means, such as the continuation of the employment in a different role or location (reinstatement), or varying the terms and conditions of employment (reengagement), are often considered by employers to be a more workable and cost-effective alternative to dismissal. Under German labour law, a court may rule that a dismissal is either effective or not effective. If a court rules that a dismissal is effective, employment terminates at the end of the notice period and the employee is not entitled to any severance (unless there is a social plan or collective bargaining agreement in place providing for severance pay). If a court rules that a dismissal is not effective, the employee must be reinstated in his or her previous position and is entitled to back pay starting from the end of the notice period.



France's social security/gross income (SS/GI) ratio.

In contrast to the rest of the EU, the UK has, on the whole, fewer restrictions on termination of employment and, as a result, reinstatement and reengagement of an employee is less common. In most cases, employees are simply paid their normal pay during the notice period.

Pay and bonuses

Public unease about levels of remuneration—particularly for financial services employees affected by the global financial crisis in 2008—has led to large financial institutions aligning their compensation practices. This is to ensure that they comply with the FSB Principles for Sound Compensation Practices and is an attempt to curb pay for bankers and other workers in the sector.

In the UK and elsewhere in the EU, financial services institutions must cap the absolute amount that is paid in bonuses to bankers. There are also provisions to claw back bonuses of senior risk takers and the requirement to defer part of bonus payments—the period of deferral dependent on the seniority and position of the employee within the firm. France and Germany also have a combination of caps, claw back and deferral mechanisms for bankers' remuneration and bonuses, while Spain and Italy both regulate the amount that can be paid in the financial sector. However, salaries and bonuses are only a part of the cost of employment. Income tax and social security contributions can represent a large proportion of an employer's total bill and relocating an employee to another EU member state could carry significant added cost.

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Regulation is not the only thing governing corporate behaviour. Local customs, reputational issues and employee expectations are also crucial

Income taxes for employees vary widely across the world. The highest-earning individuals in Singapore are taxed at 22 per cent, which compares favourably with 45 per cent in Germany, France, Spain and the UK.

In the UK, employer social security is set at 13.8 per cent of salary, while France imposes a 43 per cent tariff just for the employer's share. That is a notable cost increase, especially for banking and financial firms that offer large salaries to senior executives who will expect equal take-home pay upon relocation.

By contrast, in the US, social security rates are considerably lower at 6.2 per cent up to an income cap as well as an additional 1.45 per cent for employee Medicare costs, although few younger employees expect to personally gain anything from the social security system, viewing it simply as another tax on their income.

What's the alternative?

Of course, Europe is not the only alternative post-Brexit location. Indeed, Professor Dr. Marcel Fratzcher, president of the German Institute for Economic Research, expects London to remain the pre-eminent European financial centre, but he adds: "No question, London will suffer from Brexit, but I don't think the Euro area, or the EU, will be the main beneficiary. I fear that a lot of financial activity will move to New York or to Asia, as a result. So Europe, overall, will be a loser."

Outside of the EU, North America and Asia may look like attractive destinations. In contrast to Europe, Singapore and the US have, on the whole, relatively fewer regulations on pay, union representation is limited and there are no works councils. The ancillary costs of employment are also low. In the US, social security and Medicare costs for employers are 7.65 per cent of payroll.

In Singapore, social security costs range from 7.5 per cent to 17 per cent, with a further contribution to the Central Provident Fund for pensions dependent on age, salary and residency. In addition, given the focus on bringing more jobs back to the US under the current Trump administration, there may be additional economic incentives to relocate employees to the US.

But regulation is not the only thing governing corporate behaviour. Local customs, reputational issues and employee expectations are also crucial factors to be considered.

US employees often have little protection against being dismissed. Termination by both employee and employer is 'at will' in nearly every state unless, for example, the employer and employee enter into an agreement for a fixed or definite term of employment, or agree to a contractual notice period or the workforce is unionised (which is rare in many industries).

What's more, non-compete clauses aiming to prevent employees moving to competitors are enforceable only to the extent that they are deemed reasonable and are banned or otherwise restricted in a number of states. Large US employers pride themselves on retaining staff to such an extent that firings are not very common, unless there are specific circumstances.

Key questions and tips for employers

Do the proposals trigger a collective redundancy exercise?

Does the relocation exercise give rise to a TUPE (or equivalent) transfer?

Can relocation clauses be invoked in lieu of making redundancies?

Is there a European and/or domestic works council(s) that has to be consulted?

Consider how Brexit might impact upon operations and staffing needs. Where appropriate, reassure employees that the organisation is following the situation closely. Let them know who they can speak to if they have Brexit-related concerns.

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In France, employer social security contributions are up to 22 per cent.

Striking a new balance

To relocate existing employees, employers should not assume that they can rely on a mobility clause in the employment contract. If redundancies are necessary, a fair redundancy consultation process must be followed and redundancy payments made. Employers may also have obligations under the Acquired Rights Directive and the Posted Workers Directive (or equivalent legislation).

Whatever form Brexit takes, it is likely to usher in changes to the way that firms operate, both in the UK and in their international markets. These changes are unlikely to prompt a mass exodus at one given point in time; they are likely to be gradual and will depend on the course that exit negotiations take. There is no indication of a single cutoff point after which all EU nationals will be expected to leave the UK, and companies should expect to rebalance operations rather than shut up shop in London entirely.

Tax, social security and the employment regime are just a few factors that are being considered; another key business consideration is the effect of Brexit on education.

Companies are closely watching the potential impact on graduate schemes, as Brexit could stymie the supply of EU students seeking higher education in the UK and thus the longer-term talent pool available to them.

Ultimately, it is critical to prepare for these changes with a review of operations, including an assessment of the implications of employee relocation. But any decisions are unlikely to be straightforward and will require detailed analysis and expert advice.

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