BREXIT Transitional Arrangements and Public International Law

Analysis for Linklaters LLP

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Executive Summary

- There is no international law requirement that there be transitional provisions made when there is a withdrawal from a treaty. However, there is significant practice in various areas of international investment law, including international trade law and international human rights law, of having provisions in a treaty establishing transitional arrangements.

- Many of these treaties have specific transitional provisions to protect certain rights and interests, such as investments.

- The notion of acquired rights is recognized as a principle of international law.

- Acquired rights have generally been widely defined in terms of a variety of property rights with an assessable monetary value.

- The extent of these rights can be considered to include elements that are relevant to the financial sector, such as licences.

Scope

On 23 June 2016, voters in a referendum in the United Kingdom (UK) voted to leave the European Union (EU), an organisation of which it had been a member of since 1973. Whilst the official process of leaving the EU does not commence until the UK ‘triggers’ Article 50 of the Treaty on the Functioning of the European Union (TFEU), there is concern about how existing rights and interests might be protected in the transitional period before the UK formally exits the EU.

The concern being addressed in this paper is that of the financial sector in London. The specific aspects of this concern arise primarily in relation to UK companies conducting financial services in other EU Member States (directly or through subsidiaries and branches), and EU companies conducting such services in the UK in the same way. These are generally regulated through the granting of licenses by authorities in the UK and across other EU States. There are also issues arising for companies from third States which operate in the UK.
There are 3 specific phases to BREXIT that are relevant in terms of law:

- The period between the referendum and triggering Article 50;
- The period between triggering Article 50 (which contemplates a two year period) and the agreement between the EU and the UK;
- The period, if any, after the agreement between the EU and the UK, and before its entry into force.

This paper is primarily concerned with the first two phases, due to their effect on decision-making in the finance sector.

This paper is focused on the issues as to whether there is a legal basis or precedent in international law that requires transitional measures for businesses in the financial services sector or similar situations; and the consequences of BREXIT in terms of acquired rights. It examines international law in respect of the interpretation of treaties, and by drawing analogies from other areas of international law which could help inform this issue. This paper does not purport to provide a thorough investigation of all international legal issues deriving from the UK’s leaving the EU and it does not explore issues of EU law.

Principles of Treaty Law

Whilst the scale of BREXIT as a withdrawal from an international organisation might be unprecedented,¹ the principles of international law concerning withdrawal from a treaty remain applicable.² Many of these principles are set out in the Vienna Convention on the Law of Treaties (VCLT), which is considered to reflect customary international law³ (and so legally binds all States) in the areas considered here.

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² In multilateral agreements, the terms ‘withdrawal’ and ‘denunciation’ are used interchangeably and give rise to the same legal consequences. One scholar notes: ‘[d]enunciation denotes a unilateral act by which a party terminates its participation in a treaty; lawful denunciation of a bilateral treaty terminates it. Although denunciation is also used in relation to a multilateral treaty, the better term is ‘withdrawal’, since withdrawal from a multilateral treaty will not, normally, result in its termination. While ‘denunciation’ is used in relation to treaties as a technical term, non-lawyers may see it as carrying undertones of its ordinary, condemnatory meaning. For this reason it should be avoided, if at all possible.’ A. Aust, Modern Treaty Law and Practice (3rd ed, 2013) 245.
³ The general recognition of some parts of the VCLT forming part of customary international law is reflected in Gabčíkovo-Nagymaros Project, Hungary v Slovakia, (1997) ICJ, paras 42-46 and 99. Similarly, see Legal Consequences for States of the Continued Presence of South Africa in Namibia [South West Africa] (1971) ICJ, para 94, where the ICJ considered that the rules in the VCLT dealing with treaty termination ‘may in many respects be considered as codification of existing customary law’.
The core relevant international law principles are:

- The specific terms of a treaty prevail, as interpreted in accordance with that treaty and the VCLT.\(^4\)
- Treaties are interpreted ‘in good faith in accordance with the ordinary meaning to be given to the treaty in their context and in light of its object and purpose’.\(^5\)
- State parties to a treaty are under an obligation to perform a treaty in good faith.\(^6\) This obligation continues to apply for so long as the treaty is in force, so it survives the notice of withdrawal and continues to apply until such time as the treaty is no longer in effect.\(^7\)
- There can be no justification under internal laws for a failure to perform obligations under the Treaty.\(^8\)
- Customary international law obligations on a State continue to apply even after withdrawal from a treaty.\(^9\)
- Reciprocity of rights and obligations is normally provided for in a treaty.\(^10\)

In this instance, there is a specific term of the treaty, being Article 50 of the TFEU, which makes provision for a Member State to leave the EU. It provides a number of procedural requirements that the Member State and the EU must fulfil. It refers to the withdrawal agreement or the expiration of a 2 year period as the point in which the provisions of the EU Treaties stop applying to the Member State. Principles of treaty interpretation will apply to the TFEU and all other relevant treaties, as well as to the withdrawal agreement.

In the situation where the UK and the EU have agreed on a withdrawal agreement and during the time (if any) between that agreement and its coming into force, all parties have an obligation to act in good faith so as not to frustrate the object and purpose of that treaty.\(^11\) The UK and the EU cannot rely on their own internal laws

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\(^4\) Article 42(2) VCLT: ‘The termination of a treaty, its denunciation or the withdrawal of a party, may take place only as a result of the application of the provisions of the treaty or of the present Convention. The same rule applies to suspension of the operation of a treaty’.

\(^5\) Article 31 VCLT.

\(^6\) Article 26 VCLT: ‘Every treaty in force is binding upon the parties to it and must be performed by them in good faith’. This is known as *pacta sunt servanda*.

\(^7\) *Alleged Violations of Sovereign Rights and Maritime Spaces in the Caribbean Sea (Nicaragua v. Colombia)* (2016) ICJ, para 39.

\(^8\) Article 27: ‘A party may not invoke the provisions of its internal law as justification for its failure to perform a treaty.’

\(^9\) Article 43 VCLT: ‘The invalidity, termination or denunciation of a treaty, the withdrawal of a party from it, or the suspension of its operation, as a result of the application of the present Convention or of the provisions of the treaty, shall not in any way impair the duty of any State to fulfil any obligation embodied in the treaty to which it would be subject under international law independently of the treaty.’

\(^10\) *Certain Norwegian Loans, France v Norway, Jurisdiction* (1957) ICJ.

\(^11\) Article 18 VCLT.
as a justification not to apply the agreement and must continue to apply any general customary international law rules (such as those of treaty interpretation) that apply.

Therefore under the international law of treaties, these specific provisions of the TFEU apply. However, the TFEU makes no substantive provisions regarding transitional measures. Accordingly, the principles of international law apply.

Withdrawal and Transition

Withdrawal from a treaty leads to the termination of that treaty as between it and other parties to it. With a multilateral treaty, such as the TFEU and the Treaty on European Union, it does not terminate the treaty entirely, only as between the UK and the EU. While there is no international law requirement that there be transition provisions made when there is a withdrawal from a treaty, there is significant practice of having provisions in a treaty for withdrawal and for transitional periods.

In many areas of international law, there are provisions for transition after notification of withdrawal. For example, in the area of international investment law, many of the bilateral investment treaties (BITs) include transitional arrangements. Our review of over 100 UK BITs\(^\text{12}\) indicates that they normally provide for transition arrangements. Typical terminology in these BITs is:

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\text{This Agreement shall remain in force for a period of ten years. Thereafter it shall continue in force until the expiration of twelve months from the date on which either Contracting Party shall have given written notice of termination to the other. Provided that in respect of investments made whilst the Agreement is in force, its provisions shall continue in effect with respect to such investments for a period of [10-20] years after the date of termination and without prejudice to the application thereafter of the rules of general international law.}\]

Therefore the BIT has a specific duration, though it continues to apply indefinitely after the expiration of that time. It allows a party to withdraw by notifying the other party. It provides for the continued effect of the treaty provisions past the

\[^{12}\text{Available at: http://investmentpolicyhub.unctad.org/IIA/CountryBits/221. The only exception is that of the BIT with Gambia.}\]

termination of the treaty, for a set period of time, with regards to investments having been made whilst the agreement was in force (see further below).

Similarly, the recently concluded Canada–EU trade agreement (CETA)\(^{14}\) provides:

[I]n the event that this Agreement is terminated, the provisions of Chapter Eight [Investment] shall continue to be effective for a period of 20 years after the date of termination of this Agreement in respect of investments made before that date.\(^{15}\)

Most human rights treaties provide for transition provisions on withdrawal. For example, Article 58(1) of the European Convention on Human Rights (ECHR) provides:

A High Contracting Party may denounce the present Convention only after the expiry of five years from the date on which it became a party to it and after six months’ notice contained in a notification addressed to the Secretary General of the Council of Europe, who shall inform the other High Contracting Parties.

Similarly, Article 78(1) of the American Convention on Human Rights (ACHR) provides:

The States Parties may denounce this Convention at the expiration of a five-year period from the date of its entry into force and by means of notice given one year in advance. Notice of the denunciation shall be addressed to the Secretary General of the Organization, who shall inform the other States Parties.

However, some human rights treaties do not contain withdrawal provisions, such as the International Covenant on Civil and Political Rights (ICCPR). This was relevant for North Korea when they sought to withdraw without success.\(^{16}\) In that instance the general international law provisions of the VCLT apply, as set out above.\(^{17}\)

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\(^{15}\) Article 30.10.


\(^{17}\) See Baruch Ivcher Bronstein vs. Peru, IACHR, 6 February 2001, para 29: ‘A unilateral act of a State cannot divest an international court of jurisdiction it has already asserted; the American Convention contains no provision that would make it possible to withdraw recognition of the Court’s contentious jurisdiction, as such a provision would be antithetical to the Convention and have no foundation in law. Even supposing a State could withdraw its recognition of the Court’s contentious jurisdiction, formal notification would have to be given one year before the withdrawal could take effect, for the sake of legal certainty and
Therefore, a period of two years transition after notification of withdrawal, as under Article 50, falls within the normal range of transition periods within international law.

**Types of Transitional Provisions**

There may be a range of transitional provisions in a treaty. These can include special protections for some aspects of rights or obligations that existed in the treaty, as is shown by State practice.

International investment law provides a number of important protections for foreign investments, which remain ongoing obligations after the withdrawal. This is seen, for example, in the UK BITs considered above, where a longer transition period is provided for investments made whilst the treaty was in force. This reflects an acknowledgement of the importance of safeguarding investments from the direct impact of treaty withdrawal, especially in relation to fair and equitable treatment, and full protection and security of investment. Anthony Aust confirms this when he notes that ‘If a treaty concerning a cooperative project is bilateral it will usually contain a transitional provision, which keeps the treaty alive until the project has been completed and provides for certain obligations to continue indefinitely’.18

Similarly, EU trade and investment treaties allow a longer transition period for any trade and investment issues arising before the withdrawal. For example, in CETA it provides:

> Notwithstanding paragraphs 1 and 2, a claim may be submitted under an agreement listed in Annex 30-A in accordance with the rules and procedures established in the agreement if: (a) the treatment that is object of the claim was accorded when the agreement was not suspended or terminated; and (b) no more than three years have elapsed since the date of suspension or termination of the agreement.19

Other EU trade treaties have similar provisions protecting investments in the context of a denunciation of the trade agreement. For example, the EU-Singapore Free Trade Agreement provides for the termination of the agreement,20 and, with regard to investments, provides:


19 Article 30.8 CETA.

20 Article 17.13, EU-Singapore Free Trade Agreement: ‘1. This Agreement shall be valid indefinitely. 2. Either Party may notify in writing the other Party of its intention to terminate
In the event that this Agreement is terminated pursuant to Article 17.13 [Duration], this Chapter shall continue to be effective for a further period of twenty years from that date in respect of covered investments made before the date of termination of the present Agreement. This Article shall not apply in the case of the termination of provisional application of this Agreement and this Agreement does not enter into force.\(^{21}\)

This position is not limited to bilateral treaties. For example, the Energy Charter Treaty 1994 provides:

The provisions of this Treaty shall continue to apply to Investments made in the Area of a Contracting Party by Investors of other Contracting Parties or in the Area of other Contracting Parties by Investors of that Contracting Party as of the date when that Contracting Party’s withdrawal from the Treaty takes effect for a period of 20 years from such date.\(^{22}\)

Also, Article 127(2) of the Rome Statute of the International Criminal Court\(^ {23}\) clearly extends the obligations of a withdrawing State. In particular it provides:

A State shall not be discharged, by reason of its withdrawal, from the obligations arising from this Statute while it was a Party to the Statute, including any financial obligations which may have accrued. Its withdrawal shall not affect any cooperation with the Court in connection with criminal investigations and proceedings in relation to which the withdrawing State had a duty to cooperate and which were commenced prior to the date on which the withdrawal became effective, nor shall it prejudice in any way the continued consideration of any matter which was already under consideration by the Court prior to the date on which the withdrawal became effective.\(^ {24}\)

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\(^{21}\) Article 9.9. See also Article 19 of the EU-Vietnam Free Trade Agreement: Agreed text as of January 2016.

\(^{22}\) Article 47(3) Energy Charter Treaty.


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In addition, in human rights law, transitional provisions tend to sustain the obligations of the State even after that State withdraws from the treaty. The intention is to overcome situations where a State attempts to avoid obligations that would have emanated during such time as the treaty was still in place for that State. For example, Article 58(2) of the ECHR provides that:

Such a denunciation shall not have the effect of releasing the High Contracting Party concerned from its obligations under the Convention in respect of any act which, being capable of constituting a violation of such obligations, may have been performed by it before the date at which the denunciation became effective.\(^{25}\)

What is retained after the withdrawal is the obligation of the State with regard to violations that took place whilst the ECHR was still in force.\(^{26}\)

Further, Article 317 of the United Nations Convention on the Law of the Sea (UNCLOS) expressly provides protection for situations created when the treaty was in force within the context of withdrawal (which is expressly provided for by the Convention).\(^ {27}\) It provides:

2. A State shall not be discharged by reason of the denunciation from the financial and contractual obligations which accrued while it was a Party to this Convention, nor shall the denunciation affect any right, obligation or legal situation of that State created through the execution of this Convention prior to its termination for that State.

3. The denunciation shall not in any way affect the duty of any State Party to fulfil any obligation embodied in this Convention to which it would be subject under international law independently of this Convention.

This would appear to build on the provisions in Article 70 of the VCLT.

Therefore, it is clear that there is a considerable body of international law, for both bilateral and multilateral treaties, that have transitional provisions which continue protection of rights after withdrawal. Many of these examples include investment

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25 See also Article 78(2) of the ACHR.
27 Article 317(1) UNCLOS: ‘A State Party may, by written notification addressed to the Secretary-General of the United Nations, denounce this Convention and may indicate its reasons. Failure to indicate reasons shall not affect the validity of the denunciation. The denunciation shall take effect one year after the date of receipt of the notification, unless the notification specifies a later date.’
and trade treaties. This could be relied on in relation to transitional provisions for the withdrawal agreement between the UK and the EU.

It is also of note that transitional measures were indirectly referred to by the UK High Court in *Miller v Secretary of State for Exiting the EU* in November 2016, when it stated, in relation to rights capable of replication in the law of the UK:

> We consider that the claimants are correct in their submission that it is the ECA 1972 which is the principal legislation under which these rights are given effect in domestic law of the United Kingdom; and that it is no answer to their case to say that some of them might be preserved under new primary legislation, yet to be enacted, when withdrawal pursuant to Article 50 takes place.²⁸

This appears to hint at the need to have clear, established measures in place ahead of withdrawal to ensure the protection of those rights. The mere promise that such legislation would be adopted does not suffice.

### Acquired Rights

The issue becomes what types of rights are able to be protected after withdrawal from a treaty. Article 70 (1)(b) of the VCLT provides:

> Unless the treaty otherwise provides or the parties otherwise agree, the termination of a treaty under its provisions or in accordance with the present Convention… does not affect any right, obligation or legal situation of the parties created through the execution of the treaty prior to its termination.

Lord McNair commented on this issue:

> In so far as the provisions of a treaty have already been executed and have had their effect before the termination, they have passed beyond the sphere of the operation of the termination; something has been done; for instance, territory has been ceded, persons or movables have been surrendered, and in many cases new rights and statuses have been created which, although they owe their origin to the treaty, have acquired an existence independent of it; the termination cannot touch them.²⁹

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²⁸ *Miller v. Secretary of State for Exiting the EU* [2016] EWHC 2768 (Admin). This is now on appeal to the UK Supreme Court.

²⁹ A. McNair, *The Law of Treaties*, (1961) p 531. This book was published eight years prior to the VCLT but probably reflects customary international law, as expounded in Article 70 (1)(b) of the VCLT.
McNair is referring to the possibility that rights (or obligations) that have arisen from a treaty could have some continuing force beyond the termination (by withdrawal) of a treaty. He has also commented:

> Respect for acquired rights … is a legal doctrine which can be said to have already attained [in 1957] a large measure of recognition as a general principle of Law.  

To support this view of the existence of customary international law on acquired rights, the Permanent Court of International Justice (PCIJ), in its advisory opinion on *German Settlers in Poland* noted that ‘private rights acquired under existing law do not cease on a change of sovereignty’. Similarly, in 1926 in *German Interests in Polish Upper Silesia*, the PCIJ noted how the principle of vested rights was one that ‘as the Court has already had occasion to observe, forms part of generally accepted international law’. In these instances, as in many others, the issue was not about rights in relation to withdrawal from a treaty but about the treatment of foreign nationals. A similar situation may arise in relation to successor States to a treaty in some instances.

A core issue is what types of rights are included within “acquired rights”. Daniel O’Connel defines “acquired rights” (in his case in relation to successor States) as:

> [A]ny legal interest, other than the personal freedom to pursue an avocation, which is reducible to monetary terms. Hence, real and personal estate of all kinds, including choses in action and equitable claims, are comprehended in the notion ‘acquired rights’. Political advantages, such as rights to public office, and certain economic advantages such as industrial or commercial monopolies have not been treated as acquired rights. It is, of course, necessary that the right be properly vested under the municipal law of the predecessor State and sufficiently evidenced.

Thus the ‘essence of an “acquired right” is that it should be a vested right, rather than a contingent expectation, and that it should have an economic value, which suggests that it should be capable of being transferred’. As Vaughan Lowe notes (in relation to expropriation of property of foreign nationals):

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31 *German Settlers in Poland* (1923) PCIJ.
32 Lord McNair above n28, 18.
An ‘acquired right’ must be treated as a ‘right’: it cannot simply be ignored. That does not mean that the right cannot be confiscated, cancelled or interfered with. As a matter of international law, all States have the right to take the property of foreign nationals as long as it is for a public purpose, and the taking is not unlawfully discriminatory, and the taking is accompanied by proper compensation. The duty to respect ‘acquired rights’ is simply the duty to treat them in accordance with international law.\(^\text{36}\)

The notion of acquired rights is closely associated with the concept of ‘property’ and ‘investment’. In international investment law, the types of acquired rights tend to relate to the definition of ‘investment’. This usually includes an array of property, for example:

(a) “investment” means every kind of asset and in particular, though not exclusively, includes: (i) movable and immovable property and any other property rights such as mortgages, liens or pledges; (ii) shares in and stock and debentures of a company and any other form of participation in a company; (iii) claims to money or to any performance under contract having a financial value; (iv) intellectual property rights and goodwill; (v) business concessions conferred by law or under contract, including concessions to search for, cultivate, extract or exploit natural resources.\(^\text{37}\)

The case law of the European Court of Human Rights (ECtHR) under Article 1 of Protocol 1 is relevant as it includes within the definition of “property” or “possessions” in that Article, ‘movable and immovable things, including intangibles such as intellectual property, contracts, judgments, licences and public benefits’.\(^\text{38}\) In Slivenko v Latvia, the ECtHR extended this further:

Possessions can be existing possessions or assets, including claims by virtue of which the applicant can argue that he or she has at least a legitimate expectation of acquiring effective enjoyment of a property right.\(^\text{39}\)


\(^\text{39}\) Slivenko and Others v. Latvia (App no. 48321/99) 2002, para. 121
So it would seem that under the practice of the ECHR, claims will be protected if they are enforceable or based on a justified expectation concerning the existence of a property right.40

From this, it would seem that “acquired rights” includes a wide range of types of property: real property including leases; personal property, intellectual property, including patents and copyrights; business goodwill; interests in companies (stocks, shares, etc.); contractual entitlements; pension entitlements linked to contributions; deposits in bank accounts; and judgments and arbitral awards.41

This is quite extensive and could be considered to include the types of financial rights and interests of the financial sector. In particular it would seem to include to the establishment of branches in the EU of UK financial institutions, and vice versa, whether as subsidiaries or through leases of property, and through the granting of licences that are ‘reducible to monetary terms’ (as O’Connel defined them).

It is of note that in most of these examples, the rights in issue are rights of non-State actors, such as individuals and corporations, rather than rights of other States which are party to the treaty. This is also consistent with the position of double taxation treaties, where the rights holders are individuals who pay taxes.42

Indeed, Article 43 of the VCLT provides:

The invalidity, termination or denunciation of a treaty, the withdrawal of a party from it, or the suspension of its operation, as a result of the application of the present Convention or of the provisions of the treaty, shall not in any way impair the duty of any State to fulfil any obligation embodied in the treaty to which it would be subject under international law independently of the treaty.

This provision refers to the customary international obligation on a State which withdraws from a treaty to continue to act to protect those who have rights or obligations under the treaty. These rights include acquired rights.

The principle of acquired rights is, therefore, recognised as a matter of customary international law binding on all States. They would apply during a transitional period unless the withdrawal agreement provided otherwise. The interpretations given by investment tribunals and the ECtHR apply to the UK irrespective of its


membership of the EU.\(^43\) This creates safeguards against the restriction or change of the legal situation of those with acquired rights.

Conclusions

The UK remains bound by its international legal obligations under, for example, human rights law and international investment law, as well as under customary international law. This is the international legal position both now, during and after BREXIT.

The position of the financial sector is likely to be regulated primarily through the specific terms of the withdrawal agreement between the EU and the UK. There is a clear and consistent precedent in a range of areas of international law, and in particular, in international investment and trade law, of having transition measures in place to safeguard investments. Moreover, the UK, the EU and its Member States have an obligation, under international law, to protect acquired rights. The extent of these rights can be considered to include elements that are relevant to the financial sector.

\(^{43}\) This is also relevant in terms of possible claims that might be made after withdrawal from the EU, which would be more likely to occur under BITs and the ECHR than to any other court or tribunal.