



Brexit

Key issues for insurance

1 February 2020

Background

On 31 January 2020 (at midnight CET, 11pm UK time, **exit day**), the UK ceased to be a member state of the EU, and the European Communities Act 1972 – the statutory basis for giving effect to EU law in the UK – was repealed. This is a profound change, but its immediate impact on UK law and regulation is limited in two important ways.

- Under the UK-EU agreement on the UK's withdrawal from the EU (the **Withdrawal Agreement**), virtually the whole of EU law remains "applicable to and in the UK" from exit day until at least 31 December 2020. The Withdrawal Agreement calls this the "transition period". Here, we call it the "**implementation period**", following terminology used in the European Union (Withdrawal Agreement) Act 2020 (the **Act 2020**). The 2020 Act implements the Withdrawal Agreement into UK domestic law.
- Under the European Union (Withdrawal) Act 2018 (the **2018 Act**), all the EU law that applies in and to the UK immediately before the end of the implementation period (a substantial proportion of all UK regulation) will continue in force as UK domestic law (with some modifications) unless and until it is replaced or amended by new UK legislation. Under powers contained in the 2018 Act, the UK government has already issued a large number of statutory instruments to amend that "on-shored" body of law, and make it fit for purpose as domestic UK legislation in a post-Brexit environment. These statutory instruments are due to come into force at the end of the implementation period.

The Withdrawal Agreement provides for the implementation period to end on 31 December 2020, unless the UK and EU agree, by 1 July 2020, that it should be extended for a further one or two years. The UK government has indicated that it does not wish to seek such an extension, and the 2020 Act states that the implementation period ends on 31 December 2020.

Deal or no deal?

The implementation period gives the UK and EU a time-limited opportunity to negotiate the terms of their future relations in respect of trade and the other areas that are currently regulated by EU law. At the end of the implementation period, any given area of UK-EU relations either will or will not be regulated by a new UK-EU agreement (a **future relationship agreement**).

When the Withdrawal Agreement was being negotiated, "deal or no deal?" was used to refer to the fact that at the point when the UK ceased to be an EU member state, there would either be no agreement on the terms of the UK's withdrawal (and so effectively a legal vacuum in UK-EU relations), or the UK would enter a transition period in which, for the duration of that period, the status quo would be largely preserved. At the end of the implementation period, it is possible that the UK and EU will have reached agreement on all the aspects of their future relations that will be governed by future relationship agreements, or none of them, but it is also quite likely that they will have reached agreement on some, but not on others, so that the question "deal or no deal?" can only be answered for each

individual topic or sector. Indeed, in some areas it may take time before it is clear whether the UK and EU will seek to reach a bilateral agreement at all, rather than, for example, simply relying on the provisions of existing multilateral instruments like the WTO rules.

It will therefore necessarily take time for clarity on any possible "deal" outcomes to emerge. The shape of "no deal" outcomes is more predictable, but here too there is some uncertainty, since an agreement reached in one area may have effects that spill over into areas that are not explicitly addressed by it.

Insurance authorisation

Deal. During the implementation period, the UK will retain many of the benefits and burdens of EU membership. UK insurers, which have passporting rights, will be able to continue to exercise them.

Passporting allows a firm authorised in one EEA member state to carry on business in any other EEA member state by way of a branch or on a cross-border services basis with the firm relying on its home state authorisation and without being required to be authorised locally.

Following the end of the implementation period, the expectation is that these passporting rights will be lost.

The Political Declaration agreed by the UK and EU alongside the Withdrawal Agreement, which sets out the ambitions of the UK and EU in respect of future relationship agreements, loosely sketches out the possible nature of the long-term UK-EU relationship which they hope will be agreed by the end of the implementation period.

The Political Declaration suggests that access to each other's financial services markets may be provided on the basis of "equivalence" after the implementation period (assuming a future relationship agreement is finalised in time). However, in the case of insurance, any such equivalence would be of fairly limited benefit and would not provide any of the benefits which passporting rights currently do.

Therefore, UK insurers who wish to carry on doing business in the EEA and write new business will need to consider alternative options. These could include:

- setting up a new licensed entity within an EEA member state which could then seek to passport into other EEA member states;
- obtaining authorisation for one or more local branches although such branches would not have passporting rights;
- acquiring a local authorised insurer within the EEA; or
- writing business through local fronting insurers and then reinsuring back to the UK.

Finally, consideration needs to be given to existing business written by a UK insurer (perhaps on a passporting basis) in the EEA prior to the end of the implementation period. Absent any trade or other agreement which exempts business already written, depending on the local laws in the relevant EEA country, it could be illegal for the UK insurer to service that business (e.g. pay claims) following the implementation period.

Options to deal with this prior to the end of the implementation period could include:

- transferring this existing business by way of a portfolio transfer or Part VII transfer to a new EEA insurer which could then carry it on (time permitting);
- merging the UK insurer into a new EEA insurer on a cross-border basis so that the business ends up in the surviving new entity (time permitting);
- converting the UK insurer into an SE and then redomiciling that entity to a member state within the EEA, allowing it to service existing business (time permitting); or
- if there is no branch in the relevant member state, out of which the business has been written, establishing a branch and seeking local authorisation for it.

A number of insurers appear to be adopting a policy of wait and see, or have tried to introduce so-called Brexit continuity clauses into policies (although query how effective these may be), or have got themselves comfortable that, in those EEA countries in which they have written business, they may be permitted to continue to write that business.

No deal. On a "no deal", UK insurers (and insurance brokers for that matter) would lose their passporting rights immediately. This is the so-called "cliff-edge" scenario.

In such a situation, it is likely that many of the mechanisms referred to above (such as Part VII transfers) could no longer be used as there would likely no longer be any mutual recognition of these arrangements.

Also, if the UK insurer has not already taken steps to establish a new EEA platform so it can write new business, there will be a time lag (perhaps a considerable one) before it can do so and put in place an alternative solution (as noted above). In the case of Lloyd's, it has established an underwriting platform in Brussels to write EEA risks.

In addition, the UK insurer may not be permitted to service existing policies in certain EEA countries and its ability to do something about this will have been significantly curtailed, assuming there is anything which can be done at all at this point in time.

However, a number of EEA countries, including France and Ireland, have unilaterally passed laws to provide transitional relief for varying time periods in respect of certain permitted activities, such as settling existing obligations.

Next steps UK insurers should actively step up their contingency planning, in particular their no deal Brexit planning, although if there is to be a no deal Brexit, their ability to do something about this is (as noted above) now seriously limited.

One area on which insurers will need to focus is the extent to which they may need to "repaper" existing contracts. For example, they should consider what steps need to be taken to terminate (in whole or in part) distribution agreements so that they do not end up writing new business in a country in which they are not permitted to do so following Brexit. In addition, consequential changes are likely to be required to be made to a number of contractual arrangements to reflect the fact that the UK will no longer be a member of the EU.

We would be very happy to discuss in more detail the implications of Brexit, and what contingency planning options might be available.

Contacts

Martin Mankabady

Partner

D +44 20 7246 7162

M +44 7507 878665

martin.mankabady@dentons.com



Michael Wainwright

Partner

D +44 20 7246 7735

M +44 7811 330 585

michael.wainwright@dentons.com



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