



NEXT STEPS: NOTICE ON CONSEQUENCES OF BREXIT IN (RE)INSURANCE SECTOR

The European Commission (the “**Commission**”) published a number of notices to stakeholders in different sectors on 8 February 2018, on the consequences of Brexit for financial services. Each notice is essentially a three page warning with a clear message that “preparing for the withdrawal is not just a matter for EU and national authorities but also for private parties”. This briefing looks at the points raised by the Commission in the notice specific to the (re)insurance sector (the “**Notice**”).

Key Points

The Notice does not raise new issues. We anticipate that most of the issues mentioned in the Notice will already be on the radar of those UK insurers who are currently operating on the basis of passporting into the EU, given the Brexit contingency planning that they are already undertaking, under the oversight of the PRA.

The Notice is clear that, in the absence of legal certainty provided by a withdrawal agreement establishing another exit date and subject to any transitional arrangements, all EU primary and secondary law will cease to apply to the UK from 30 March 2019, 00:00h (CET) (the “**Withdrawal Date**”). The UK will then become a ‘third country’, with the consequences specified below.

Authorisations

- UK insurers will no longer benefit from the Solvency II authorisation to provide services in the EU i.e. they will lose their “passport” and will no longer be allowed to provide services in the EU, including through online sales.
- Branches of UK insurers in the EU will be treated as branches of third-country insurance undertakings. They will need an authorisation in the Member State of their activity to be able to continue to do business but this authorisation will not grant the entity passporting rights to conduct business across the EU Member States.

UK insurers who currently use passporting rights to provide insurance in the EU are actively considering their options, including authorisation of branches or subsidiaries in their chosen EU27 location, or moving the head office of an Societas Europaea (“SE”) to a jurisdiction within the EU.

- EU-27 subsidiaries¹ can continue to operate as EU insurers on the basis of their authorisation in the EU Member State of their establishment and subject to their compliance with the EU rules, including in terms of governance, risk management, and outsourcing.

¹ Legally independent companies established in EU-27 and controlled by or affiliated to insurers established in the UK.

- UK reinsurers will have to comply, for their EU business, with the conditions set by the EU Member State in which they carry out their activity. These conditions cannot be more favourable than those applying to reinsurers from the EU, but they may be less favourable and may well differ between EU Member States: for example, Member States are free to require the pledging of assets or the establishment of a branch by the third country reinsurer.
- The above requirement in respect of UK reinsurers is without prejudice to any equivalence decision on the UK that may be adopted by the EU, whereby reinsurance contracts concluded with undertakings having their head office in the UK must be treated by EU Member States in the same manner as reinsurance contracts concluded with undertakings authorised in accordance with Solvency II.

We are aware that reinsurers are actively considering the extent to which reinsurance can be conducted in the EU27 from the UK on a non-admitted basis. We would expect the UK to achieve reinsurance equivalency but this requires an application to be made to the EU and we are not aware of any such application to date. It is likely that the European Insurance and Occupational Pensions Authority (“EIOPA”) would conclude that it cannot consider any such application until such time as the UK has become a third country and it is not clear how any such hiatus would be dealt with.

Insurance Contracts

- The loss of EU authorisation may affect the ability of UK insurers to continue performing certain obligations and ensure service continuity with regard to contracts concluded before the Withdrawal Date.
- The Notice states that according to the Solvency II Directive, insurers are required to take measures to ensure that contracts can continue to be serviced. To this end, the Notice recommends that insurers should assess the impact of Brexit on their operations and contract portfolios and, also in cooperation with the relevant national supervisors, identify and mitigate risks.

UK insurers should already have undertaken a Brexit impact assessment with oversight from the PRA. We are aware that UK (re)insurers are actively considering their ability to service pre-Brexit contracts post-Brexit. For those (re)insurers for whom a transfer of pre-Brexit business to an EU27 authorised entity is not feasible, there are significant challenges in many EU jurisdictions. Although some Member States have already indicated a position on continuity of contracts, the EIOPA position is not helpful, as mentioned in the Notice, and a more pragmatic approach from EU27 regulators is hoped for (allowing for policyholder protection) which would treat pre-Brexit contracts as valid until termination (without possibility of renewal) and would not impose sanctions on insurers who service these contracts (whether before or after expiration of any transition or implementation period).

Other Aspects

- **Information disclosure:** The Notice states that Articles 183-186 of the Solvency II Directive require that policyholders/customers should be informed about the impact on their rights and on the provision of insurance services that may emerge from Brexit, including the upcoming loss by the relevant insurer/intermediary of its EU authorisation.

Our reading of these provisions of Solvency II is somewhat narrower. Communications with policyholders and others affected is an important part of a Part VII process and the move of the head office of an SE. Where such processes are not being undertaken we anticipate that UK insurers will want to communicate with affected policyholders, but are unlikely to do so wholesale until there is more clarity around any timing and nature of any transition/implementation period.

- **Group supervision:** (Re)insurers operating in the EU but which are part of a group whose parent undertaking is authorised in the UK will be subject, in the absence of UK equivalence, to the Solvency II provisions empowering EU supervisory authorities to require a worldwide group solvency or to apply “other methods” aiming to ensure appropriate group level supervision including the establishment of a holding company with head office in the EU.

Again, it is difficult for insurers to proceed with detailed planning in this respect until there is more clarity as to whether or not the UK will seek/obtain equivalence.

- The Notice flags that any group-level internal model covering a UK group operating in the EU, approved by the PRA before the Withdrawal Date will no longer be recognised in the EU as of the Withdrawal Date, and will require a new application and approval by an EU-27 supervisor. Any entity-level internal model for a subsidiary of an UK insurer established in one of the EU-27 Member States and approved by the supervisor of that Member State will remain valid.

We are aware that UK insurers are having discussions with regulators in EU27 jurisdictions about part of the application for authorisation of a third country branch/subsidiary, and the applications of internal models will form an important part of such discussions.

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