BREXIT SECTOR VIEWPOINT
INSURANCE

The UK's insurance and long-term savings industry is the largest in Europe and the fourth-largest in the world.

The insurance market developed in the UK over the last 200 years depends for its success upon, among other things, efficient regulation, access to world-class talent and the ability to underwrite risk around the world, including in EU markets.

Brexit presents the UK insurance sector with the prospect of restricted access to talent and European markets but the opportunity for progressive regulatory reform.

RISKS AND OPPORTUNITIES OF BREXIT

Access to world-class talent:

Given the complexity and bespoke nature of much of the business written in the UK, the market attracts some of the world's top insurance talent.

In the short term, at least, much of the existing insurance expertise is expected to stay. Lloyd's of London, for example, has confirmed that its central operations will remain in London, even though it intends to move some of its operations to Brussels during 2018.

Longer term, one challenge may be in reconciling the need for high-quality insurance staff with the Government's policy on immigration controls. The UK risks losing talent to other markets with less rigid border controls.

Restricted access to the single market:

'Passporting' currently allows UK insurers and reinsurers to conduct cross-border business in the EU relying on a single home state licence (and EU insurers can conduct business in the UK on the same basis). If, post Brexit, the EU and UK fail to negotiate terms close to 'free access', UK-based firms might be forced to shift some of their business to the EU. Meanwhile, international insurers whose European operations are headquartered in the UK are likely to be looking carefully at the location of their European hubs.

For UK insurers with policyholders in EU Member States, the risk, post-Brexit, is that they will no longer be licensed to deliver services in those countries unless they go through the onerous process of establishing an authorised branch in each country. Not doing this may leave insurers unable to pay out on claims, and EU policyholders without valid insurance.

UK and EU insurers' freedom to operate in the other's territories therefore hinges on future reciprocal agreements between the UK and EU.

Freedom to set own rules:

The UK, under Brexit, should be able to reduce some of the burdens that UK insurers encounter with the EU's Solvency II Directive

Some argue that changing the UK regime would allow UK-headquartered groups to become more competitive outside the EU. In practice, however, there are other considerations:

- The UK was the driving force behind much of the content of Solvency II and is unlikely to reform the current regime radically. UK insurance companies also suffered massive upheaval and expenditure to comply with the EU directive and, for the most part at least, are not agitating for

"The UK's insurance and long-term savings industry manages over £1.6 trillion in investments and pays tax of almost £12 billion. If it is not carefully managed, the impact of Brexit on the insurance industry could make a big dent in the UK's economic strength."

GEOFFREY MADDOCK, PARTNER, INSURANCE, HERBERT SMITH FREEHILLS LLP

BREXIT VIEWPOINT
INSURANCE SECTOR OUTLOOK

a significant rewriting of the rules.

- The UK is renowned internationally as having regulation and supervision of the highest standard. Putting that reputation at risk to further the competitiveness of UK groups in overseas markets is unlikely to be in the UK's long-term interests.
- For the UK to be assessed as "equivalent", it will undoubtedly need to follow Solvency II closely. The benefits of an equivalence determination under Solvency II are, however, limited. Some UK insurers, at least, would favour a less onerous regulatory regime over equivalence.

More generally, UK insurers will wish to consider whether they would be better served if the UK maintained close alignment with EU rules, including in non-industry specific areas (eg data privacy).

Despite its name, the UK government's "Great Repeal Bill" will seek to ensure that most EU law currently applicable in the UK remains UK law after Brexit, with only essential changes initially to make the law work after Brexit and change after that being a gradual process. This cannot completely replicate the present situation as, for example, UK legislation cannot bind the remaining EU Member States to recognise aspects of UK law which are inherently cross-border in nature (such as, for example, the validity of cross-border portfolio transfers).

PREPARE FOR THE UNKNOWN

Despite the uncertainty, insurers must prepare for life outside the EU and keep a close watch on the shifting political landscape.

Many firms are making plans on the assumption that passporting rights will be lost and that exit terms agreed by the Government (if any) will fall short of providing free access to the single market. Some are considering moving some or all of their business outside the UK, possibly (like Lloyd's) setting up a new European subsidiary as a hub for their European affairs. Given that there may be no transitional period once the UK extricates itself from the EU, and as insurance firms can take a year or more to restructure, few are prepared to wait and see what the Government's negotiations might deliver.

Our technical and industry experts, experienced in shaping legislative and regulatory reform, began preparing for Brexit 18 months before the referendum. They are working with insurance clients on various questions, including:

- What business do we do now and where do we do it? Who are our customers and where are they located?
- What licences are needed to carry on that business and how will that change if passporting rights are lost?
- How can we best reorganise our operations to meet the challenges presented by the loss of passporting rights?
- How much time do we need to ensure that any reorganisation is implemented in time for the UK's withdrawal from the EU?

Upfront planning can help insurers to prioritise their mitigation strategies. It can also inform lobbying to Government and industry bodies in the lead-up to exit negotiations.

Insurance groups with investment management operations can refer to our Asset Management sector outlook for further guidance.

"The worst case scenario for insurers would be having to meet the full rigour of Solvency II standards, without having ready access to EU markets."

BARNEY HINNIGAN, PARTNER, INSURANCE, HERBERT SMITH FREEHILLS LLP

KEY CONTACTS

Geoffrey Maddock
Partner
T +44 2074 662 067
geoffrey.maddock@hsf.com

Barnaby Hinnigan
Partner
T +44 2074 662 816
barnaby.hinnigan@hsf.com

Alison Matthews
Consultant
T +44 2074 662 765
alison.matthews@hsf.com

Paulino Fajardo
Partner
T +34 91 423 4110
paulino.fajardo@hsf.com