

Planning for life after Brexit

The contractual considerations for insurers if Britain votes to leave the EU



Stephen Browning
Clyde & Co

In five weeks' time, the UK may have voted to leave the European Union. For insurance businesses – whether based in the UK or elsewhere in the European Economic Area (EEA) – Brexit would have significant regulatory implications. It would also have potentially serious commercial consequences (particularly for some UK-based businesses), the nature and extent of which could vary enormously depending on the mechanism for post-Brexit UK access to EU markets (and vice versa).

If there is a vote to leave, then from the date on which the government gives notice of the UK's intention to withdraw from the EU the clock will start ticking towards an automatic exit two years later, unless within that period an agreement on the terms of the withdrawal is concluded or the other 27 member states unanimously agree to a longer period to negotiate such terms.

The result will be a lengthy period of uncertainty while negotiations between the UK and the rest of the EU take place. But businesses will not be able to sit and wait for the outcome. Contingency planning around the regulatory implications and other consequences will need to be progressed. Despite all the uncertainties, it makes sense for insurance businesses to be engaged now in a preliminary exercise of identifying issues and considering options – perhaps for them to undertake some more detailed contingency planning in certain areas.

In an exercise of this kind there are numerous matters to consider. Perhaps the most immediate is the possibility of adverse effects on insurers' liquidity, investments and solvency positions (and credit ratings) in consequence of volatility in financial markets and any downgrade in

the UK's own credit rating and how these might be mitigated.

Regarding a business's key contracts, the issues list will have two sections: existing contracts and new ones.

In existing contracts (including distribution, outsourcing, IP licensing, IT and financing agreements and standard terms and conditions), provisions that deal with a number of matters could be examined to assess how Brexit might affect the rights and obligations imposed by the provisions and whether amendments may be necessary or desirable (if they are possible).

The provisions that could be examined include those regarding territorial scope (with respect to distribution obligations and non-competition clauses, for example); references to European laws or legal concepts; regulatory reporting and compliance with other regulatory obligations; data protection; financial condition; termination (including any material adverse change clauses); force majeure and law and jurisdiction. Plus, there is the question of whether any existing contract is so dependent on European legal provisions or concepts that it might become wholly or partly impossible to perform.

Termination rights

For any new contracts signed before the vote, the list will extend to the possibility of including Brexit-related termination rights or excluding Brexit from any material adverse change or force majeure clauses and to considering how the possibility of Brexit might impact the drafting of other provisions.

Top of the list for many businesses will be a consideration of the steps that could be taken in order to secure ongoing access to EEA markets (in the case of a UK firm or group) or to the UK market (in the case of a non-UK firm or group), if the UK's future trading relationship with the EU did not provide for the continuation of passporting.

These steps could include such things as obtaining local authorisations for existing EEA branches of a UK insurer, the establishment (or acquisition) of an EEA insurer by a UK insurer (or a group containing only a UK insurer) that currently passports across the EEA or switching passports from a UK insurer to an EEA insurer where a group contains both kinds of carrier. Of course, the operational changes and costs that would be associated with such steps would also need to be considered to assess their viability in the light of the profile of the particular business and its current (or any revised) post-Brexit business strategy.

Terms and conditions for product wordings and product pricing will also feature highly on the list. Alterations may be needed, although how extensive these might need to be would depend on the product, the form that Brexit takes and the extent of associated changes to English law in the years ahead.

Insurance being a "people business", human resource matters will also feature highly. These include: how any changes to the work permit system and other employment laws might affect

the ability of UK citizens to work elsewhere in Europe, or of persons from elsewhere in Europe to work in the UK, or result in increased employment costs; and how any structural changes to secure ongoing access to markets might affect the location of senior management and other staff.

Regulation

Another topic for the list is that of prudential regulation and reporting, although it must be highly likely that, following a Brexit, the UK would maintain a Solvency II-based system (Solvency II itself being heavily based on the UK's previous risk-based regime). If this were the case, one would assume that the UK system would be assessed by the EU as "equivalent" under Solvency II. In the unlikely event of the UK system diverging from Solvency II – or of the UK maintaining a Solvency II-based system but not obtaining a grant of full equivalence for that system from the EU – Europe-wide groups headquartered in the UK might become subject to 'double supervision' under both the UK regime and Solvency II.

On the subject of regulation, the list should also include the possi-

bility of additional information being required by the UK regulators and of increased demands on the regulators themselves impacting on their speed of response to requests for approvals (for example, to changes in control) and rule waivers/modifications.

Data protection should also feature – the key issue being how cross-border data flows might need to change, depending on the approaches the UK might take to data protection regulation in a post-Brexit world.

There may be other important matters to consider, depending on the nature and structure of the individual business. However, with limited exceptions (such as implementation of hedging arrangements and possibly, pursuit of an M&A transaction that could have Brexit-related benefits where there are good non Brexit-related strategic or financial reasons for the deal), any contingency plans drawn up in the near future (whether before June 23 or afterwards, if there is a vote to leave) should almost certainly not be acted on until matters become considerably clearer. ■

Stephen Browning is a partner at Clyde & Co

