

12 July 2018

Chris Hobley  
Director of Market Access and Budget  
Department for Exiting the European Union  
9 Downing Street  
London  
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Dear Mr Hobley

### Issues of legal uncertainty relating to insurance business in the context of Brexit

The role of the Financial Markets Law Committee (the “FMLC” or the “Committee”) is to identify issues of legal uncertainty, or misunderstanding, present and future, in the framework of the wholesale financial markets which might give rise to material risks, and to consider how such issues should be addressed.

In the light of the U.K.’s withdrawal from the E.U. (“Brexit”), the FMLC has been focusing on particular industries and issues which give rise to material risks. One area of focus has been the effect of Brexit on the insurance industry. As the Financial Policy Committee of the Bank of England (the “FPC”) has observed, the insurance industry is especially exposed to risks caused by the withdrawal of certain rights to conduct business in the E.U.<sup>1</sup>

At present, an insurer authorised in the U.K. is entitled to conduct business in other Member States by way of an establishment or through the provision of cross-border services. Following a “hard” Brexit, U.K. insurers will lose these passporting rights and will be regarded as Third Country entities. The FMLC has previously written about Third Country regimes generally and about the complexities of identifying the *locus* of services provided under E.U. financial services legislation.<sup>2</sup> The FMLC has also published a paper recently on the establishment of an insurer in an E.U. Member State (the “Establishment Paper”), discussed further below.<sup>3</sup>

As part of its work in this context, the Committee resolved to examine the process of insurance business transfers under Part VII of the Financial Services and Markets Act 2000 (“Part VII”). Part VII establishes a framework for the use of court-sanctioned schemes to transfer insurance business from one regulated entity to another. In preparation for the loss of their passporting rights, many U.K. insurance firms are applying under Part VII to transfer certain contracts to entities established in E.U. Member States. The FPC anticipated an increase in applications in advance of the withdrawal date, and the Bank of England has warned the High Court of the same.

The Committee’s research group considered a number of aspects of the Part VII regime to identify potential legal uncertainties, and determined that the better view is that the

<sup>1</sup> See Bank of England, *Financial Stability Report Issue No. 42* (November 2017) and Bank of England, *Financial Stability Report Issue No. 43* (June 2018).

<sup>2</sup> FMLC, *Issues of Legal Uncertainty Arising in the Context of the Withdrawal of the U.K. from the E.U.—the Provision and Application of Third Country Regimes in E.U. Legislation* (13 July 2017), available at: <http://fmlc.org/report-u-k-withdrawal-from-the-e-u-13-july-2017/>.

<sup>3</sup> FMLC, *Issues of Legal Uncertainty Arising in the Context of the Establishment of an E.U. Insurer in another Member State*, (12 July 2018), available at: <http://fmlc.org/report-establishment-of-an-e-u-insurer-in-another-member-state-12-july-2018/>.

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High Court and regulatory authorities are well-placed to manage these processes within the context of Brexit. The Committee did conclude, however, that an issue which has already been identified in other areas will be particularly challenging in this field, namely the question of whether and when an insurer is providing services in another Member State.

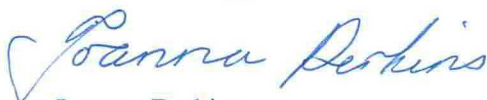
Currently, careful analysis is required to determine on a case-by-case basis whether an insurer authorised in the U.K. will in fact be providing services in the E.U. when it performs its pre-Brexit contracts of insurance. The FMLC's Establishment Paper explores the issue of delineating between acting through an establishment and providing services in a Member State. To an extent, this issue was addressed by an Interpretive Communication adopted by the European Commission in 2000. That Interpretive Communication predates, and differs from, Directive 2009/138/EC of the European Parliament and of the Council of 25 November 2009 on the taking-up and pursuit of the business of Insurance and Reinsurance (the "**Solvency II Directive**") in respect of the test for establishment.<sup>4</sup> This has created legal uncertainty for insurers, particularly as they prepare for Brexit. More detailed analysis about this issue can be found in the Establishment Paper.

It would assist industry participants if HM Government were to raise, in the course of its Brexit negotiations, the potential need for a revised or further Interpretive Communication from the European Commission in relation to insurance services. This would assist insurance firms in their Brexit planning, including in the preparations underlying their Part VII applications to achieve compliance with U.K. and E.U. rules post-Brexit.

Finally, these uncertainties may be an opportunity to provide guidance to foreign firms on the provision of services into the U.K. After Brexit, the U.K. will no longer be bound by the Solvency II Directive. In the U.K., E.U. insurance firms will be treated as foreign firms and therefore subject to the authorisation requirements in the Financial Services and Markets Act 2000. Any additional guidance on characterisation issues—i.e. determining when an insurer is effecting or carrying out contracts of insurance in the U.K.—would reflect best practice and aid the mitigation of disruption risks in advance of Brexit.

I and Members of the Committee would be delighted to discuss the issues raised in this letter and the enclosed paper with you further. Do not hesitate to contact me should you wish to arrange a meeting or if you have any questions.

Yours sincerely,



Joanna Perkins  
FMLC Chief Executive<sup>5</sup>

*Cc: Eral Knight, Ministry of Justice; Sean Martin, Financial Conduct Authority*

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<sup>4</sup> The differences in the conditions for branch establishment in the Insurance Interpretive Communication and the Solvency II Directive are explored in greater detail in paragraphs 2.6 to 2.8 of the Establishment Paper.

<sup>5</sup> In view of the role of the FCA and Bank of England in the preparation for the U.K.'s withdrawal from the E.U., Sean Martin and Sinead Meany took no part in the preparation of this paper and the views expressed should not be taken to be those of the FCA and the Bank of England.