



Insurance Europe position paper in the context of Brexit

Grandfathering of existing contracts to protect customers

Executive summary

Currently, EU/EEA (re)insurers can provide contracts to customers in the UK and UK (re)insurers can provide contracts to customers in the EU/EEA through passporting - ie across borders ('Freedom of Services') and through local branches ('Freedom of Establishment'). After Brexit, passporting rights between the EU/EEA and the UK will cease. EU/EAA branches of UK based (re)insurers will become third-country branches and the status of UK branches of EU/EAA-based insurers is not clear.

The TF50 [position paper](#) "Essential principles on citizens' rights" says that the Withdrawal Agreement should protect the rights of EU27 citizens, UK nationals and their family members who, at the date of entry into force of the Withdrawal Agreement, have enjoyed rights relating to free movement under Union law, as well as rights that are in the process of being obtained and the rights the enjoyment of which will occur at a later date including, for example, pension rights.

This principle should include (re)insurers' ability to service existing contracts issued before Brexit on the basis of passporting which will continue to run after Brexit (eg life insurance, pensions, commercial package policies, travelinsurance, directors' and officers' liability insurance, etc). EU and UK citizens have rights under those contracts. Their ability to exercise those rights depends on (re)insurers' ability to service those contracts. If there are legal and regulatory obstacles preventing (re)insurers from meeting their customers' expectations, the legal uncertainty may severely disrupt EU citizens' financial arrangements. This, in turn, may lead to severe consumer detriment unless appropriate arrangements are made.

Without any arrangement to solve the problem, the transfer of portfolios will be unavoidable, even though it is a difficult and time-consuming process. Indeed, to maintain a level of protection that is equivalent to the level stated by European regulation, grandfathering is the best solution, which would allow insurers to service existing contracts under EU law.

As stated by the TF50, the Withdrawal Agreement should focus, as a matter of priority, on protecting citizens' rights. Therefore, it should ensure that citizens do not lose rights under (re)insurance and pensions contracts entered into before Brexit by passporting (re)insurers. For this reason, we recommend a 'grandfathering' arrangement for current long-term (re)insurance contracts (non-life and life insurance and pensions) that were issued while passporting was available. The grandfathering clause should go beyond the simple affirmation of the principle that insurers to continue to service existing contracts. It should also take into account the continuity of the supervisory standards related to insurance contracts, as these standards currently exist in European regulation. It is important that such a grandfathering arrangement should also apply to commercial insurance in order to avoid unnecessary disruption of the business of insured companies.

The negotiations between the EU and the UK should seek to address this issue, which is elaborated in greater detail below.

1. What are existing contracts?

Existing contracts issued by (re)insurance companies are contracts that meet the following conditions:

- Contracts concluded before the date of entry into force of the Withdrawal Agreement (or the date at which the Treaties no longer apply to the UK, if different) which give rise to obligations for either contractual party after the UK is no longer an EU member.
- Contracts issued either:
 - by a British (re)insurer through passporting to a customer residing in another EU/EEA country or who was residing in the UK at the time of sale but later moved to another EU/EEA country, and to corporate customers established in another EU/EEA country; or
 - by an EU/EEA (re)insurer through passporting to a UK-based customer or someone who later moves to the UK and to corporate customers established in the UK.

Examples of such contracts include:

- Long-term life insurance and pension contracts. These are set up to run for many years. Contracts taken out by citizens before Brexit are intended to provide benefits possibly decades in the future. It is impossible to predict when each contract will end, as the duration of payments will depend on the longevity of the individual insured.
- Multi-year general insurance contracts, such as some types of commercial package policies. Businesses may take these policies out to give themselves longer-term certainty and they may be in force when the UK leaves the EU.
- Insurance policies with a policy period of one year or less. Any policy purchased from a passporting insurer by a business or private customer for up to a year before the UK leaves the EU is likely to be in force on the date of Brexit.
- Passporting insurance contracts that have expired at the date that the UK leaves the EU. Such contracts may well have claims outstanding under them, where the customer has either reported the claim and is awaiting settlement or has not yet reported the claim. For example, liability policies can give rise to long-tail claims years or even decades after the policy has expired.
- Cross-border reinsurance contracts. These may either be in force when the UK leave the EU or have outstanding claims under them.

2. What do the EU/EEA passporting rights allow?

Under the EU/EEA framework, passporting rights allow EU-based (re)insurers to:

- issue contracts cross-border and/or through branches
- service contracts sold to customers in the EU/EEA who move, later on, to another EU/EEA country

Contracts issued on the basis of passporting are subject to prudential supervision by the home member state and conduct of business supervision by the host member state. In addition, depending on the national law where a policy has been issued, the policy may be protected by different compensation measures in the home member state of the contract's scheme.

3. How does Brexit affect customers of existing contracts?

(Re)insurers that do business on a passporting basis between the UK and the EU/EEA and try to continue to service existing contracts, for example by paying claims, would no longer have authorisation to do so and would breach national law in those host countries where a license is required. They could face high penalties and possible sanctions under the law of host countries, regardless of the fact that the contracts between the (re)insurers and the customers are still valid. In other words, without portfolio transfers or grandfathering, (re)insurance firms would have to break the law in order to fulfil their contractual obligations.

In this situation, customers would not be able to:

- claim for risks covered by their contracts
- prevent paid losses from being treated as income in their country of residence and taxed accordingly
- pay premiums that would allow them to continue to contribute to their policies (eg pensions)
- access specific compensation measures foreseen in the home member states of their contracts

Since insurers — who have appointed a legal representative under Article 145 or 152 of the Solvency II Directive — are required to maintain a legal representative in the country concerned until the relevant national competent authority is satisfied that the business has been fully run off, without grandfathering consumers will not be able to bring legal action in national courts against a lawfully appointed representative of the insurer. Additionally, the payment processes between insurers and reinsurers under existing contracts might be affected.

It is difficult to assess precisely the number of customers that would be affected, however research is in process to give some indication of the number of citizens that would be impacted.

4. Why is ‘grandfathering’ the best solution for existing contracts?

‘Grandfathering’ existing contracts would offer a permanent solution to ensure customers can continue to benefit from the contracts they have lawfully entered into until those contracts run off, possibly decades after Brexit. Grandfathering would protect customers from adverse consequences as a result of Brexit and prevent as far as possible consumer detriment and severe disruptions to customers’ personal situations, such as financial planning for retirement.

Other potential options would not protect customers as much as ‘grandfathering’ because:

- The transfer of individual contracts or books of policies to entities in another jurisdiction can be complex, lengthy and may require approval by courts/supervisory authorities and/or customers. National competent authorities reviewing transfers would face a very high workload and would probably not be in a position to authorise such transfers in time for Brexit. For instance, currently it takes the UK Prudential Regulation Authority between 12 and 18 months to approve new entities. In addition, transfers of insurance portfolios from UK (re)insurers to their new EU/EEA entities (and vice versa) would become unlawful after Brexit, unless the receiving entity had already been granted authorisation to conduct business in the relevant member state. Additionally, some types of policies do not exist in some countries and national competent authorities have no experience in supervising them. Some contracts relate to assets that could not be untangled without high costs for customers. Ultimately, transfers would create unnecessarily high costs with no guarantee of success.
- Transitional measures bridging the gap between the moment the UK exits the EU and the future EU-UK relationship coming into force are important. However, in particular for life insurance contracts, they will not resolve the problem of servicing contracts written under passporting. A transitional period is likely to be for a maximum period of 2/3 years, whereas contractual obligations under passported contracts could run for decades after Brexit. Furthermore, they require that the future relationship is agreed and precisely defined.

These options do not address the problem of being able to continue to fulfil contractual promises made to EU/EEA citizens who move to the UK, and UK citizens who move to the EU/EEA, either pre- or post-Brexit.

5. How to allow for grandfathering of existing contracts?

We recommend that the UK and the European Union agree on the grandfathering of existing (re)insurance and reinsurance contracts as part of the Article 50 negotiations under the Citizens’ Rights chapter.

A comprehensive approach to this issue must take reinsurance contracts and retrocession into account. Reinsurance enables insurers to reduce their underwriting risks, allowing them to strengthen their solvency, expand their capacity to absorb different types of customer risks and to reduce the volatility of their earnings, enabling them to offer lower prices to their customers. Especially in respect of life and pensions, reinsurance contracts run for decades and a permanent solution to ensure service continuation until their termination has to be found. It is therefore absolutely necessary that grandfathering provisions apply to reinsurance contracts, in order to avoid cliff-edge scenarios for customers.

Grandfathering would mean:

- Recognition that the rights and obligations of the parties to (re)insurance contracts written lawfully under passporting continue.
- (Re)insurance contracts in force at the date that the Treaties cease to apply to the UK would continue to be in force until they expire in accordance with contractual provisions.

- Legal obstacles to the ability of a party to an (re)insurance contract to enforce a right or discharge a responsibility under the contract would not apply.
- (Re)insurers who have appointed a legal representative under Article 145 or 152 of the Solvency II Directive would maintain a legal representative in the country concerned, until the relevant national competent authority is satisfied that the business has been fully completed.
- Regulatory responsibility for contracts should remain as it is at present, i.e. prudential regulation would remain a home state responsibility and conduct regulation a host state responsibility. Supervisory liaison could be ensured by establishing an EU27/UK committee, possibly under the auspices of EIOPA.
- The UK and the EU27 would need to agree on a disputes resolution mechanism.
- Special provisions would be needed for contracts between the UK and EEA member states that are not EU members.

The European Council's negotiating directives mandate the Commission to negotiate an Agreement that ensures any goods placed on the market before the withdrawal date will continue to be made available after the withdrawal date (paragraph 31). It is important that services are given similar consideration as soon as possible. We note the intention that services be covered by a subsequent set of negotiating directives: we would reiterate that time is of the essence and insurers and customers need certainty as soon as possible.

For additional information, please contact Rosa Armesto, Head of Public Affairs & Communications (armesto@insuranceeurope.eu, tel: +32 2 894 30 62).

Insurance Europe is the European insurance and reinsurance federation. Through its 35 member bodies — the national insurance associations — Insurance Europe represents all types of insurance and reinsurance undertakings, eg pan-European companies, monoliners, mutuals and SMEs. Insurance Europe, which is based in Brussels, represents undertakings that account for around 95% of total European premium income. Insurance makes a major contribution to Europe's economic growth and development. European insurers generate premium income of €1 200bn, directly employ over 985 000 people and invest nearly €9 900bn in the economy.