At the time of writing, July 31st 2018, there stands approximately 11 weeks between the deadline by which the United Kingdom (UK) and the European Union (EU) must reach some agreement as to what their post-brexit relationship will be. While the date of Britain's departure from the EU is 29th March 2019 (with a proposed transition period lasting until 31st December 2020), a deal must be agreed by this October because it will require ratification in the individual parliaments of the 27 other EU member states, a process which will at its very least take 6 months.

It had been hoped that the EU would, because of the value of London's status as a financial centre and because of the substantial outgoing trade the EU has with the UK, facilitate Britain's exit by allowing it to maintain some of the benefits of EU membership without having to bare some of the associated responsibilities. Indeed, the mainstream pro-Brexit factions made this their rallying call. This however, has not happened. Instead, the EU has stood resolute in its position that its primary concern is the integrity of its internal single market and that the UK cannot "cherry pick" those aspects of market access which benefit it and discard those that do not.

Withdrawing itself from a cornerstone of the global economic system of which it was a prime architect was never going to be an easy proposition but there had been an overarching feeling in the City of London that the dreaded no deal scenario (where the UK has to revert to World Trade Organisation (WTO) rules, impose tariffs on its closest markets and lose its status as a preferred supplier of financial services as its regulatory system diverges from that of those markets) would never happen and that even though key aspects of the Brexit pitch were unrealistically optimistic, the worst that would happen would be a bad deal on everything else with a carve out for financial services, an industry which represents one fifth of the British Economy. This too, has not happened and the UK is closer to a no deal than anyone ever imagined it would be at the time of the referendum in June 2016.

How did we get here?

To give readers some context, for the better part of 40 years, Britain's Conservative party has been at war with itself over the UK's relationship with the EU. Like most Western conservative parties it is a coalition of global free market capitalists at one end and nationalist social conservatives at the other. The tension between these two strands over Britain's place in the EU and in the world led to the June 2016 referendum which was itself was an attempt by the conservative party leadership to silence the anti-EU faction of the party because, while vocal, they are a minority. Needless to say that attempt did not go as planned.

The current British Prime Minster, Theresa May, attempted to unite the fighting factions of her party, efforts which have culminated in a formal statement of Government Brexit policy on the future relationship between the United Kingdom and the European Union a White Paper) which was released 4 weeks ago The White Paper was supposed to unite the Government around compromise positions allowing the country to present a united negotiating front to the EU. Instead, there was a flurry of Government resignations when it was released and it is widely agreed that the proposed negotiating terms represent the

worst of all worlds, making the UK a taker of EU rules while limiting its access to European markets.

No deal or a bad deal

There is an overarching sense that the British Government's demands on certain aspects of the post Brexit relationship with the EU will be untenable from the EU's perspective and that as a result negotiations will break down and Britain will leave the EU without a deal. Even if that were not to happen, Britain's financial services industry is braced for a bad deal.

The reason for this is that passporting, the coveted system which allows British insurance businesses to establish or provide services in other EU member states free from new regulatory hurdles in the host state, is not on the list of UK Government wants. This has come about largely from the realisation that there was not much point suggesting to the EU that it be retained as it would require adherence to the regulatory standards of the EU which the British Government was not prepared to accept.

Subject to successful negotiations, the UK will instead seek an enhanced equivalence regime which it is hoped will allow mutual recognition of financial services products, instruments and processes. The concern though is that all existing equivalence regimes are staunchly in favour of the EU and - considering the current tone and trajectory of the negotiations - there is no evidence to suggest that the EU will be much more facilitating of British aspirations in this regard.

More broadly, there will be no regulatory alignment between the EU and UK. As indicated in a previous article in this publication, financial stability is of too great importance to a country to have its terms dictated by a third party, which is what the EU will be once the UK leaves it.

There is also in the Government proposals a reference to a possible "cross border provision" for some financial services subsectors, proposals on this are vague and it is thought that the difficulty which the Government had in agreeing what it wants has lead to a lack of clear stated objectives in this area.

Needless to say, the Government's proposals, which are supposed to be Britain's best case Brexit scenario, have gone over like a lead balloon in the insurance industry. Lloyd's CEO Inga Beale called them "very disappointing" and reaffirmed Lloyd's belief that mutual regulatory recognition would have been the best approach. She also reiterated that the insurance market's newly established Brussels hub is ready to step in and allow Lloyd's coverholders to continue access to continental markets regardless of the outcome of Brexit.

Shortly after the release of the White Paper, Britain's financial services regulator the Financial Conduct Authority (FCA) announced publicly that it was now making plans for a no deal scenario, including implementing regulatory programmes for the 8500 European financial services businesses which are providing services in the UK to be granted temporary permission under a new regime to allow them to continue conducting business. It is of course hoped, though it is not at all clear, that the EU will reciprocate in this regard.

Second Referendum?

There are increasingly respected voices calling for a second referendum on the terms of any final proposed deal – when a former cabinet member recently joined those calls, the overwhelming retort was 'what question would we ask' as opposed to the in principle arguments that were being used 6-12 months ago.

Former Lloyd's chairman John Nelson was the most recent to add his voice to this chorus labelling the Government's White Paper the "worst possible scenario" for the insurance industry. By any measure, there is no majority in the British Parliament to sanction a no-deal and the government's proposed deal is disliked not only by the financial services industry but also by Brexiteers and Remainers alike. If Parliament were to reject both options then the default position would be to remain in the EU however by so doing Parliament would be acting contrary to the expressed opinion of the 2016 referendum. It is therefore thought that to rid itself of the responsibility, parliament may put the final decision back to the electorate at another referendum on the terms of the deal. There are however a myriad of logistical and technical obstacles to this and it is not at all clear that it will happen.

The here and now

So what does all this mean for financial services and for the risk management industry in particular. As a law firm and a consultancy working actively in the regulatory space, it has come as something of a surprise to us at EC3 Legal and EC3 Consultants that we are receiving a spike in instructions, even from some fairly big insurance intermediary players, regarding both re-domicile in the EU and seeking advice on contract continuity*. This has come about largely because the wait and see approach that some of the more nimble intermediaries had been taking, in part because the idea of a no-deal scenario or the loss of passporting was so unthinkable that the risk of it coming to fruition made planning for it a waste of resources, has now come to an end.

With most major regulatory and industry bodies now advising that they are planning for a no deal scenario, these are the preparations that are finally being made as even the smallest businesses scramble to secure continued EU market access and the continued ability to write business in the EU. It should be noted that even if there is a deal, the Government White Paper sets out that they will not be seeking regulatory alignment or mutual recognition and so the insurance industry is now in full preparation for a genuine and fundamental change in it's relationship with continental European markets and for a relationship which is both more restricted and more distant than is has been.

*insurance contract termination clauses can often be triggered by changes in the regulatory status of the parties



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