Solvency II: Cross-border provision of services

Robert Chaplin	Hello and welcome. I'm Robert Chaplin, one of Slaughter and May's corporate insurance partners. With me is Beth Dobson, our PSL Counsel for the insurance practice. This is our overview of the regulatory regime for third country branches and cross-border provision of services. For more information please see chapter 12 of our Solvency II App. If you don't already have the App please email solvency.two@slaughterandmay.com to request access. Under Solvency II, EU insurers benefit from the freedom to provide services and freedom of establishment across the EU – so-called "passporting rights". Notification requirements apply within the EU for the cross-border provision of services and to set up a branch in another EU member state. Now that the UK has left the EU, passporting rights no longer apply to UK insurers in respect of EU member states or vice versa. The option to establish a third country branch does still exist, however, and there is some potential scope for the provision of services on a cross-border basis, which we will explore in this podcast. A transitional regime currently operates in the UK in respect of policies written by EU firms prior to the end of the Brexit Transition Period, and reciprocal transitional arrangements have also been put in place by most EU Member States, although the length of the transitional arrangements varies. In the UK, EEA firms which elected to enter the Temporary Permissions Regime are deemed to have a UK authorisation for up to three years from 31 December 2020. In addition, the Financial Services Contracts Regime allows firms to run off their existing insurance business in the UK (without writing new business) for 15 years.
Beth Dobson	According to the PRA, prior to Brexit over 600 EU firms held passporting permissions to write business in the UK, although not all of these passports were actually being used. 190 have entered the UK's temporary permissions regime and many of these are expected to apply for permanent authorisation under the UK's third country branches regime before the TPR expires. The key requirements for an overseas firm (from the EU or elsewhere) to obtain authorisation for a UK branch are:

	• Firstly, the PRA's threshold conditions must be satisfied, including requirements as to legal status, location of offices, conduct of business and suitability • Additional conditions specific to third country branches must also be met, principally that there must be a representative of the applicant resident in the UK with authority to bind it, it must have authorisation in its home state to effect and carry out contracts of insurance and it must have UK assets as specified by the PRA rules • A number of capital requirements must be satisfied at branch level, which we will come on to; and • The branch undertaking must maintain adequate worldwide financial resources. The main features of the regime for third country branches reflect the Solvency II regime, as amended to reflect the UK's departure from the EU. The Solvency II regime does not set out requirements for third country branches which carry on only reinsurance activities but the UK regime applies, in the most part, equally to pure reinsurance branches.
Robert Chaplin	Looking in a bit more detail at the capital requirements which apply to third country branches in the UK, undertakings must calculate a branch MCR and SCR and cover each of these with eligible own funds. Unless the branch is a pure reinsurance branch, it must hold in the UK assets to cover the branch SCR and must deposit as security with a suitable credit institution in the UK an amount equal to at least one quarter of the absolute floor of the MCR. The undertaking must also establish adequate branch technical provisions. Calculations of branch assets and liabilities and classification of branch own funds must be carried out in accordance with applicable rules. The PRA process for authorisation of a third country branch goes beyond the satisfaction of capital requirements, however. It has emphasized – in particular in its 2018 supervisory statement on its approach to branch authorisation and supervision – that key considerations in considering an application will be the regulatory equivalence of the undertaking's home regime and the ability of the PRA to supervise the insurer. The latter consideration will be affected by the extent of supervisory cooperation between the

	PRA and the home state regulator. The PRA will also consider the degree of protection offered to UK policyholders, including in the event of an insolvency of the undertaking. De facto limits apply to the size of third country branch which the PRA will be willing to authorise. Although not a hard threshold, it has says that it expects that in general third country branches will have under £500 million of insurance liabilities covered by the Financial Services Compensation Scheme. Non-UK undertakings wishing to carry on larger operations in the UK will need to set up a UK subsidiary.
Beth Dobson	So far we have talked about the absence of passporting and the requirements for setting up third country branches. There is, however, a more fundamental question regarding when authorisation will be required for insurance activities to be carried on. In the UK authorisation to carry on a regulated activity is only required where the provider of the product or service is carrying on business in the UK. Whether or not that is the case will depend on a number of factors. Case law suggests that in considering whether a firm is carrying on insurance business in the UK the court would look at the activities carried on by the insurer as a whole, taking into account, among other things, the law governing the policy, the location of the risk, the place where the policy was entered into, the place where premiums are collected and the place where payments are made. In order to avoid breach of the UK financial promotions regime it will also be important to avoid communicating an invitation or inducement to engage in investment activity in the UK. An EEA firm wishing to write policies aimed at consumers will need to set up a branch or subsidiary but there are other business models where the firm may not need authorisation. It is not uncommon for non-UK reinsurers, for example, to reinsure risks ceded by UK insurers without having a UK authorisation. Risks insured under group policies where the parent company is in an EEA member state but some risks or subsidiaries are located in the UK is another example of where firms may wish to structure a policy so that no activities are being carried on in the UK. There are a number of ways in which this can be achieved, including “reverse solicitation”, where the person seeking the insurance makes an unsolicited request to the insurer, and structuring group insurance policies so that UK entities do not have a direct claim under the policy. A number of conditions would need to be met in either case.

Ben Kingsley	The approach of other jurisdictions to what activities require authorisation varies. In general the attitude towards reinsurance business is more relaxed than for direct insurance business. In Germany, for example, firms based in “equivalent” jurisdictions do not need authorisation to carry on reinsurance business. Germany also allows “insurance by correspondence” in the case of reinsurance, which is where at the instigation of German firm a reinsurance contract is concluded by correspondence with a primary insurer or reinsurer in a third country without the use of a German intermediary. Going forwards, cross-border insurance business between the EU and the UK will be more complicated than pre-Brexit. As with non-EU entities, it will involve a combination of the use of local subsidiaries and branches and a degree of business conducted without the need for authorisation. Other than for reinsurance, this is likely to be easier for firms seeking to write business into the UK than from the UK into the EU. This brings us to the end of this podcast. If you have any questions about third country branches and cross-border provision of services please get in touch with either of us or your usual contact at Slaughter and May.