Issues Review
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Insurers Step Up Brexit Plans in Absence of Clarity

In the absence of clarity as to what a future trade deal will look like, affected insurers have accelerated their plans to establish new EU subsidiaries

Insurers in the UK that access business in the EU are putting in place arrangements to ensure that they are able to provide insurance services in the other 27 EU countries post Brexit. The ability to continue to conduct cross-border business is a particular concern for Lloyd's, the London market and other UK-based commercial insurers. It is less of an issue for retail insurers as they principally underwrite domestic business.

This year, in the absence of clarity as to what a future trade deal will look like between the UK and the EU, affected insurers have accelerated their plans to establish new EU subsidiaries. These subsidiaries will ensure that they are able to underwrite EU business post March 2019 or after any formally agreed transition period. Small insurers, that do not have the resources to create additional companies, are forming relationships with local carriers that can front business for them in the EU.

Insurers are also addressing the possibility that, in the absence of a political solution, companies in the UK that currently make use of passporting rights will not be able to service claims on existing EU policies after Brexit. As a contingency, a growing number of companies are exploring potentially expensive Part VII transfers of existing EU business to their newly-created subsidiaries.

Rationale Varies for Domicile Choice

To date, Luxembourg and Ireland have emerged as the most popular locations for a new EU subsidiary (**see Exhibit 1**). However, no single city appears likely to challenge the position of London as Europe's principal (re)insurance hub.

Domicile choice has been driven by the specific considerations of individual insurers, including proximity to clients, the ability to attract talent, an existing presence in a location, as well as the local tax regime. The domestic regulator has also been important, particularly its approach, expertise and accessibility.

Of these, the principal driver of domicile choice has been whether there is an existing operation, such as a branch, in a particular location. Although Lloyd's has established a subsidiary in Brussels, this in itself does not appear to have attracted other London market insurers. Amlin and QBE have also selected Brussels, but this decision was largely driven by the fact that they have an existing presence there. Beazley, Aspen and XL's preference for Dublin was underpinned by the same reason, as was Chubb's decision to opt for Paris and Markel's choice of Munich.

In A.M. Best's view, there is sound rationale for this. Where companies have established branches or a material presence in a particular market, it is usually because they believe it will help them access attractive business. In addition, they will already have underwriting talent and infrastructure in place at that particular location, and they will usually have a relationship with the local regulator. These are important considerations in view of the operational and capital costs they will incur in establishing an additional subsidiary.

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The cost implications of setting up a new risk carrier in the EU are weighing on insurers and the associated operating and restructuring expenses will impact their earnings. Furthermore, the creation of an additional, separately-capitalised subsidiary may reduce the fungibility of capital across an insurance group and its capital efficiency.

In order to offset increased operational costs, A.M. Best expects insurers to grow their top line in the EU. Once an insurer has invested in a European infrastructure, it is logical from a cost efficiency point of view to use it to write more business. Turning an existing branch into a capitalised subsidiary is a means of demonstrating commitment to a particular market and, consequently, it could be positive for the insurer's standing in that market.

Insurers are also looking for ways to reduce capital requirements at these new subsidiaries and minimise trapped capital. One way to achieve this is to transfer material underwriting risk back to other group entities through reinsurance. However, this usually requires regulatory support. Regulators will also be key in determining what constitutes a meaningful presence in a particular market – the outcome of which will have operational cost implications.

In cases where an insurer does not have existing operations in an EU location, Luxembourg is proving to be an attractive domicile. The local regulator, the "Commissariat aux Assurances" (Insurance Commission), is viewed as business friendly and efficient, and Luxembourg is host to a good network of support services, such as lawyers and accountants.

In each of these chosen locations, A.M. Best expects subsidiaries to be small relative to the insurer's UK operations.

Exhibit 1
(Re)insurers - European Union Domiciles Planned

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Company Name	Domicile
Lloyd's	Belgium
MS Amlin	Belgium
QBE	Belgium
Chubb	France
Ironshore[4]	Germany
Markel	Germany
St Julians[2]	Gibraltar
Aspen	Ireland
Aviva	Ireland
Beazley	Ireland
Chaucer	Ireland
Equitable Life[1]	Ireland
Everest Insurance	Ireland
Legal & General	Ireland
NEON Underwriting[1]	Ireland
North P&I Club	Ireland
Royal London	Ireland
Standard Life[1]	Ireland
The Standard Club	Ireland
Travelers	Ireland
XL Group	Ireland
Sompo Japan Nipponkoa Insurance Inc	Luxembourg
AIG	Luxembourg
Aioi Nissay	Luxembourg
CNA Hardy	Luxembourg
FM Global	Luxembourg
Hiscox	Luxembourg
Liberty Speciality Markets	Luxembourg
RSA	Luxembourg
Tokio Marine	Luxembourg
Starr	Malta
Compre[3]	Malta
The UK P&I Club	Netherlands
Steamship Mutual	Netherlands
Chesnara	Netherlands
Admiral	Spain

Notes:
1: To be confirmed. 2: Transfer of domicile from Malta to Gibraltar. 3: Transfer of domicile of London & Leith Insurance SE 4: Refers to Ironshore International's Mergers & Acquisitions and Tax Insurance unit
Source: A.M. Best data and research

London is likely to remain one of the world's leading insurance centres and the principal insurance hub in Europe, supported by its pool of underwriting talent and access to related services. Nevertheless, the detail of any negotiated trade deal between the UK and the EU will have a longer-term impact on the UK insurance sector. Furthermore, the London market is currently under pressure from other, arguably stronger, forces, including alternative capital, market consolidation and the pressing need for process reform.

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