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Insurance & Reinsurance 2022

UK: Law & Practice
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UK

Law and Practice

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CONTENTS

1. Basis of Insurance and Reinsurance Law p.3
1.1 Sources of Insurance and Reinsurance Law p.3

2. Regulation of Insurance and Reinsurance p.3
2.1 Insurance and Reinsurance Regulatory Bodies and Legislative Guidance p.3
2.2 The Writing of Insurance and Reinsurance p.3
2.3 The Taxation of Premium p.5

3. Overseas Firms Doing Business in the Jurisdiction p.6
3.1 Overseas-Based Insurers or Reinsurers p.6
3.2 Fronting p.6

4. Transaction Activity p.7
4.1 M&A Activities Relating to Insurance Companies p.7

5. Distribution p.7
5.1 Distribution of Insurance and Reinsurance Products p.7

6. Making an Insurance Contract p.8
6.1 Obligations of the Insured and Insurer p.8
6.2 Failure to Comply with Obligations of an Insurance Contract p.9
6.3 Intermediary Involvement in an Insurance Contract p.9
6.4 Legal Requirements and Distinguishing Features of an Insurance Contract p.9
6.5 Multiple Insured or Potential Beneficiaries p.10
6.6 Consumer Contracts or Reinsurance Contracts p.10

7. Alternative Risk Transfer (ART) p.10
7.1 ART Transactions p.10
7.2 Foreign ART Transactions p.11

8. Interpreting an Insurance Contract p.11
8.1 Interpretation of Insurance Contracts and Use of Extraneous Evidence p.11
8.2 Warranties p.11
8.3 Conditions Precedent p.12

9. Insurance Disputes p.12
9.1 Insurance Disputes over Coverage p.12
9.2 Insurance Disputes over Jurisdiction and Choice of Law p.13
9.3 Litigation Process p.14
9.4 The Enforcement of Judgments p.14
9.5 The Enforcement of Arbitration Clauses p.15
9.6 The Enforcement of Awards p.15
9.7 Alternative Dispute Resolution p.16
9.8 Penalties for Late Payment of Claims p.16
9.9 Insurers' Rights of Subrogation p.16

10. Insurtech p.16
10.1 Insurtech Developments p.16
10.2 Regulatory Response p.17

11. Emerging Risks and New Products p.17
11.1 Emerging Risks Affecting the Insurance Market p.17
11.2 New Products or Alternative Solutions p.18

12. Recent and Forthcoming Legal Developments p.19
12.1 Developments Impacting on Insurers or Insurance Products p.19

13. Other Developments in Insurance Law p.20
13.1 Additional Market Developments p.20

1. BASIS OF INSURANCE AND REINSURANCE LAW

1.1 Sources of Insurance and Reinsurance Law

The Financial Services and Markets Act 2000 (FSMA) is the principal source of law governing (re)insurance in the UK. FSMA and other regulations provide the main framework for the UK's regulatory regime, but a large proportion of the law applicable to (re)insurers in the UK that became law prior to Brexit was influenced by or derived from European Community legislation, with the most significant source being EU Directive 2009/138/EC, commonly known as "Solvency II".

Solvency II has been transposed into UK law in a number of ways: through FSMA itself, in statutory instruments (the Solvency 2 Regulations 2015 (SI 2015 No 575)) and through new rules in the UK regulators' "rulebooks". Prior to Brexit, as in other European jurisdictions, (re) insurers in the UK were also subject to directly applicable regulations made under Solvency II, notably Commission Delegated Regulation (EU) 2015/35 (the "Solvency II Regulation"), which have been incorporated into English law so as to apply post-Brexit. (Re)insurers should continue to comply with relevant EU guidance issued prior to Brexit. References to Solvency II in this article are to the Solvency II Directive and the Solvency II Regulation (see **3.1 Overseas-Based Insurers or Reinsurers** and **13.1 Additional Market Developments** for further information about the impact of Brexit).

Prior to Brexit, UK legislation in respect of other specific aspects of insurance business often supplemented these sources, including the Insurance Act 2015, which came into force on 12 August 2016 and reformed insurance contract law (the "IA 2015"). Post-Brexit, all relevant legislation will derive from the UK.

The UK is a common law jurisdiction, so as well as statute, precedent judicial decisions have an impact on the development of the UK's legal system. In the context of (re)insurance, this may be particularly relevant in the interpretation of insurance contracts and in filling any gaps left by statute.

2. REGULATION OF INSURANCE AND REINSURANCE

2.1 Insurance and Reinsurance Regulatory Bodies and Legislative Guidance

Under FSMA, (re)insurers in the UK are regulated by the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA), which are responsible for authorised firms' prudential regulation and conduct supervision, respectively. UK (re)insurers are therefore often referred to as being "dual-regulated". Insurance intermediaries such as brokers and managing general agents (MGAs) are regulated by the FCA only.

The PRA Rulebook, the FCA Handbook and associated supervisory statements are important sources of rules and guidance for the financial services firms to which they apply, including (re)insurers.

The specialist (re)insurance market, Lloyd's of London ("Lloyd's"), is also regulated by the PRA and FCA, as are managing agents, and managing agents/underwriters participating in the Lloyd's market are also subject to Lloyd's supervision.

2.2 The Writing of Insurance and Reinsurance

As a result of the "general prohibition" in Section 19 of FSMA, a firm seeking to conduct (re)insurance business in the UK must obtain authorisa-

tion or permissions under Part 4A of FSMA from the PRA (unless it is exempt – see **3. Overseas Firms Doing Business in the Jurisdiction**). The FCA must consent to the PRA's granting authorisation. Insurance intermediaries apply to the FCA rather than the PRA.

To obtain authorisation, a firm must be able to satisfy the "threshold conditions" set out in FSMA on an ongoing basis. These conditions include:

- legal status – ie, being a company, friendly society or member of Lloyd's;
- demonstrating that the firm's head office and registered office are in the UK or that it carries out business in the UK;
- being adequately capitalised to conduct the (re)insurance business in question; and
- the individuals who manage the firm being fit and proper and suitably qualified to do so.

The PRA-regulated activities that are referred to broadly as "(re)insurance business" are set out in the Financial Services and Markets Act 2000 (PRA-regulated Activities) Order 2013, and include effecting or carrying out contracts of insurance (in other words, entering into or performing contracts of insurance, respectively) and managing the underwriting capacity of a Lloyd's syndicate as managing agent at Lloyd's.

A regulated activity is subject to the general prohibition to the extent that it is carried on "by way of business" in the UK. This restricts the applicability of the rules to persons who undertake the activity in a commercial context and with some degree of regularity. Assuming the activities themselves are carried out in the UK, it is irrelevant if the underlying risks are located outside the UK or if the contracts are subject to a different governing law. If the activity is not carried on in the UK, authorisation is not required under FSMA even if policyholders and/or the underlying risks are located in the UK.

Statute does not fully define the term "contract of insurance". The Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 does not set out the features that determine whether a contract is an insurance contract, so it is useful to look to the common law for this analysis. Although the regulators may determine whether a contract is a contract of insurance and therefore subject to regulation, this may be challenged in court.

A firm will need to seek PRA authorisation for each class of business it intends to write. FSMA divides insurance business into 18 classes of general business and ten classes of long-term (or life) business.

Capital and Reserve Requirements under Solvency II

UK (re)insurance companies are subject to the capital requirements contained in Solvency II, as set out and expanded upon in the PRA Rulebook. There are basic requirements that apply to all authorised (re)insurers, plus additional and different requirements for general insurers, life insurers and pure reinsurers. The PRA can impose additional capital requirements on individual firms if deemed necessary to address certain risks, such as operational or conduct risks.

The capital requirements under Solvency II consist of the minimum capital requirement (MCR – ie, the minimum amount of capital a (re)insurer needs to cover its risks) and the solvency capital requirement (SCR – ie, effectively the amount of capital a (re)insurer needs to operate as a going concern), assessed on a value at risk measure. A firm's SCR can be calculated according to a standard formula or, with PRA approval, using its own internal model. Capital requirements apply at the entity and group level. Lloyd's Solvency II

capital requirements are calculated as a whole based on its internal model and apply to the market as a whole across all Lloyd's syndicates. Lloyd's operates its own capital assessment of each syndicate, the Economic Capital Assessment, which is broadly based on Solvency II.

Solvency II and the PRA Rulebook also provide the requirements as to reserves to be maintained by UK (re)insurance companies. Reserves, or technical provisions, must be calculated in a prudent, reliable and objective manner, with the value of the technical provisions corresponding to the amount the (re)insurer would have to pay if its (re)insurance obligations were immediately transferred to another Solvency II firm. Technical provisions must represent a best estimate, as well as including an additional risk margin, calculated in the prescribed manner.

Excess of Loss

There is no different regulation specifically for writing excess of loss (XOL) layers in the UK and authorisation requirements apply equally to insurers and reinsurers. A contract of insurance includes a contract of reinsurance, although a company may be licensed as a "pure reinsurer" and therefore not permitted to write direct business. Fewer of the conduct rules apply to pure reinsurers, as the insureds are regulated insurers rather than individuals. Therefore, XOL reinsurance may be subject to lighter regulation – eg, not being subject to all the consumer conduct rules. Since the introduction of the IA 2015, which applies to business insurance and reinsurance contracts and contains the duty of fair representation of the risk, as well as specifying remedies the (re)insurer has for a breach, there has been a move away from (re)insurers being favoured under the common law on insurance contracts.

Consumers' Rights

The IA 2015 followed on from other changes to amend the common law and insurance contracts in favour of consumers, including the Third Parties (Rights against Insurers) Act 2010, which made it easier for third parties to claim directly against insurers (on liability insurance) where the insured was insolvent, and the Consumer Insurance (Disclosure and Representations) Act 2012, which curtailed an insurer's rights to avoid the contract at common law.

2.3 The Taxation of Premium

Insurance premium tax (IPT) derives from European Community law (although it has not changed as a result of Brexit) and was introduced in the UK by the Finance Act 1994 and the Insurance Premium Tax Regulations 1994.

IPT is a tax on premiums paid under all contracts of insurance, wherever written or wherever the insurer or insured is located, except those specifically exempted from IPT (which includes those where the contract relates only to non-UK risks, reinsurance or life assurance). IPT is generally payable to HMRC by the insurer (or in some cases by a taxable intermediary). In practice, groups of insurers that are UK corporates may account for IPT under a single registration, while other special registration arrangements apply to Lloyd's syndicate members, non-UK insurers and partners in a partnership.

IPT is chargeable at 12% (standard rate) or 20% (higher rate) of the IPT exclusive amount of the premium paid to the insurer by the insured (or taxable intermediary), depending on the type of insurance contract and who arranges it.

3. OVERSEAS FIRMS DOING BUSINESS IN THE JURISDICTION

3.1 Overseas-Based Insurers or Reinsurers

The starting point for firms deemed to be carrying on (re)insurance business in the UK (even if they do not have a permanent establishment in the UK, for example, by acting through agents) is that authorisation under FSMA is required.

Business Not Carried on in the UK

As noted in **2. Regulation of Insurance and Reinsurance**, a risk in the UK can be insured without UK authorisation if the regulated activity is not being carried on in the UK. It may be possible for overseas (re)insurers to arrange to carry out their business in such a way that they are not deemed to be doing so in the UK itself, thereby avoiding the need for approval under FSMA. This may not be an entirely straightforward approach, however, given that the position is not entirely certain, there is a significant amount of guidance from the regulators and case law around what activities constitute "effecting" or "carrying out" a contract of insurance and whether business is therefore being carried on "in the UK" and, under FSMA, permission may still be required for other activities connected to the main regulated insurance activities. For example, making arrangements in the UK in connection with the "effecting" of a contract of insurance is an FCA-authorised activity and would require authorisation.

Third-Country Branches

Non-UK insurers may apply for authorisation to establish a UK branch if they meet the relevant regulatory requirements to do so. There are certain distinctions under Solvency II; for example, a single branch cannot carry out both life and non-life insurance activities (subject to certain "grandfathering" provisions), and Solvency II sets no particular standards for pure reinsurers to establish a branch.

Effect of Brexit

The PRA and FCA have implemented a "temporary permissions regime" that, under certain conditions, permits non-UK European Economic Area (EEA) firms to continue to passport into the UK for a limited period. Provisions have also been implemented to preserve the validity of contracts written cross-border into the UK pre-Brexit where the EEA insurer does not intend to apply for UK authorisation. While other EEA member states have implemented broadly similar transitional provisions that allow UK-authorised firms to continue to service policyholders resident in those member states under existing contracts, the respective time periods have been set by each individual member state and vary considerably.

3.2 Fronting

There is no prohibition on fronting in the UK. Historically, the UK regulators have tended to look unfavourably on the practice, but it is possible and, indeed, a number of financial guaranty firms have entered into fronting arrangements, whereby business was written in the UK and 100% reinsured back to the parent entity.

The Financial Services Authority (FSA) – the PRA and FCA's predecessor – had concerns around counterparty credit risk of the non-UK parent and the possible risk of UK policyholders not being paid, which was perceived as less of an issue for commercial lines such as financial guarantees, particularly where obligations were collateralised. This concern was dealt with in the regulator's rulebook through a presumption that reinsurance above a certain amount of reserves assumed too much credit risk unless it could be justified and mitigated; for example, by collateral or a guarantee. In practice, the regulators would now expect retention of at least 10% of

the risk (as a general rule of thumb). This figure has also been raised more recently as "a good referential" by the European Insurance and Occupational Pensions Authority (EIOPA) in its Brexit guidance.

4. TRANSACTION ACTIVITY

4.1 M&A Activities Relating to Insurance Companies

Despite the ongoing uncertainties of COVID-19 and Brexit, M&A activity in the global (re)insurance industry remained active in the first half of 2021, which saw an increase in average deal value. The hardening of the insurance market and interest in insurance companies by private equity firms have been key drivers. The sustained low-interest environment has undoubtedly also increased pressure on (re)insurers to refine their business models, increasing scale and/or exit classes of unprofitable or non-core business.

The life insurance sector has seen considerable activity following the implementation of Solvency II, with a number of insurers exiting lines of business with higher capital requirements, such as annuities or other products with long-term guarantees. There has also been an effect on the run-off market as firms look to be as capital-efficient as possible in a low-interest, low-growth environment and offload non-core business through share sales, reinsurance or business transfers, or often a mixture of the two latter approaches. These deals can release significant amounts of regulatory capital, which the insurer can deploy elsewhere in new opportunities (see also **12. Recent and Forthcoming Legal Developments**).

The broker market is experiencing significant consolidation due to regulatory change and the challenging economic environment. However, such consolidation has faced setbacks following the US Department of Justice blocking the proposed merger between Aon and Willis Towers Watson. Deal activity in insurtech businesses has increased as COVID-19 has encouraged (re)insurers to utilise digital technology (see **10. Insurtech**).

In the non-life sector, a number of acquirers continue to be interested in Lloyd's businesses. Membership of Lloyd's gives a presence in the global (re)insurance and specialty markets using Lloyd's international licences and capital rating, thus avoiding the need for separate authorisations and individual capital requirements in each jurisdiction. 2020 saw the launch of four new "syndicates-in-a-box" (SIAB), part of Lloyd's modernisation agenda, and 2021 saw the launch of Lloyd's first environmental, social and governance (ESG) syndicate, which was established under the SIAB framework.

Much M&A activity has been driven by financial investors with plenty of capital and an interest across the full spectrum of the insurance sector.

5. DISTRIBUTION

5.1 Distribution of Insurance and Reinsurance Products

(Re)insurance distribution in the UK takes place through a wide variety of channels, including through direct sales, brokers acting on behalf of their clients in arranging (re)insurance cover, agents acting on behalf of the (re)insurer, independent intermediaries, banks (through bancassurance or partnership arrangements), various retailers in connection with retail products being sold, and increasingly online sales, often through comparison websites, particularly for motor and home insurance.

Distribution at Lloyd's takes place through brokers and through insurance agents or cover-

holders, holding binding authorities on behalf of the managing agents/syndicates for whom they underwrite. Such intermediaries have to be separately approved by Lloyd's in addition to receiving any other intermediary authorisation required in the jurisdictions where they operate. There has been significant consolidation in the broker and intermediary sector in the UK.

Regulation of distribution in the UK is based on the EU's Insurance Distribution Directive (Directive 2016/97/EU) (IDD), which replaced the Insurance Mediation Directive (Directive 2002/92/EU). The IDD aimed to improve intermediary regulation to cover all sellers of insurance, including insurers themselves, and ensure the same level of protection for consumers regardless of the distribution channel used. In the UK, intermediation by (re)insurers was already regulated and, therefore, fewer changes were required to implement the IDD. The IDD is implemented in the UK through FSMA and associated statutory instruments, as well as through the FCA Handbook.

The FCA is responsible for the authorisation and both the prudential and conduct regulation of intermediaries operating in the UK. Every person in the intermediation chain from customer to insurer must be authorised or exempt. Intermediation is defined widely to include arranging a contract of insurance, making arrangements with a view to someone entering into a contract of insurance, dealing in a contract of insurance as agent, advising on a contract of insurance or assisting in the administration and performance of a contract of insurance. A lighter conduct regime applies to reinsurance intermediation.

Rules for intermediaries range from compliance with capital and professional indemnity insurance requirements through training and competence requirements to information required to be provided to potential customers, which varies according to the type of intermediary, business and customer.

6. MAKING AN INSURANCE CONTRACT

6.1 Obligations of the Insured and Insurer

The IA 2015 reformed UK insurance contract law in relation to misrepresentation and non-disclosure in commercial contracts. It applies to all (re)insurance contracts entered into wholly or mainly for the purposes of trade, business or profession that are entered into or varied after 12 August 2016.

Duty of Fair Presentation

The IA 2015 places the insured's common law duty of full and frank disclosure on a statutory footing, imposing a duty on insureds to make disclosures in a manner that would be reasonably clear and accessible to a prudent insurer. The "accessibility" requirement is intended to prevent "data dumping" – ie, disclosing a mass of data without highlighting material considerations.

Representations of fact by insureds must be "substantially correct", and representations of expectations or belief must be made in good faith. An insured must make a "reasonable search" of the information available to them, including information held by their agents or others who are intended to be covered by the insurance.

An insured will need to disclose every material circumstance they know or ought reasonably to know, or sufficient information to put a prudent insurer on notice that the insurer needs to make further enquiries for the purposes of revealing the material circumstances.

A "material circumstance" for these purposes is anything that would, or is reasonably likely to, influence the judgement of a prudent insurer in determining whether to take the risk and, if so, on what terms.

6.2 Failure to Comply with Obligations of an Insurance Contract

In the case of commercial contracts, where the breach of the duty of fair presentation by the insured was deliberate or reckless, the insurer can avoid the contract, keep the premium and refuse to pay claims. Where the breach was not deliberate or reckless, the remedy depends on what the insurer would have done if a fair presentation had been made. If the insurer would not have entered into the contract at all, it can return the premium, avoid the contract and refuse to pay claims. If the insurer would have entered into the contract but on different terms, the contract is treated as if the different terms had been agreed. If the insurer would have charged a higher premium, the insurer can proportionately reduce the amount it pays on a claim.

In relation to consumer contracts, the Consumer Insurance (Disclosure and Representations) Act 2012 ("CIDRA 2012") requires the insurer's remedies to be proportionate to the failings of the insured.

6.3 Intermediary Involvement in an Insurance Contract

An insurance intermediary may act on behalf of the insurer or the insured. Where an insurance broker is acting on behalf of the insured, its duty is to exercise reasonable care and skill in the fulfilment of its instructions and the performance of its obligations. An insurance broker is also under a duty to carefully ascertain its clients' insurance needs and to use reasonable skill and care to obtain insurance that meets those needs, together with carefully reviewing the terms of any quotations or indications given to its clients. An insurance broker must also ensure that it explains to its client the terms of the proposed insurance to ensure the client is fully informed and satisfied that all its insurance requirements are met. An intermediary acting on behalf of an insurer must comply with the conduct of business requirements applicable to the selling of insurance.

6.4 Legal Requirements and Distinguishing Features of an Insurance Contract

At common law, there is no requirement for a contract of insurance to be in any particular form or even to be in writing, although there is usually a document (called a policy) that evidences the contract. Some insurance contracts, such as contracts for marine insurance, are required by statute to be expressed in a policy.

Insurable Interest

The Marine Insurance Act 1906 and the Life Assurance Act 1774 (which is not restricted to life insurance) require an insured person to have an insurable interest in the subject matter of the insurance. This means that, in order for an insurance contract to be valid, the person taking out the insurance should stand to benefit from the preservation of the subject matter of the insurance or suffer a disadvantage should it be lost.

The law on insurable interest differs depending on whether the contract is for non-indemnity insurance (insurance that pays out a lump sum on the occurrence of a specified event, such as death, personal accident or critical illness, regardless of the loss suffered) or indemnity insurance (which compensates the policyholder for loss suffered). In the case of non-indemnity insurance, the Life Assurance Act 1774 makes null and void any policy on the life or lives of any person(s) or on any event made by any person having no interest.

The English and Scottish Law Commissions have consulted on the topic of insurable interest at various times over the past ten years, suggesting that the law of insurable interest is complex and uncertain, and not required at all in relation to indemnity insurance. In 2016, the Law Commissions conducted a short consultation on a draft bill to reform the law on insurable interest, and published an updated draft bill on 20 June 2018. At the time of writing, the Law Commissions were analysing responses to the consultation on the updated draft bill and indicated that they will produce a report with final recommendations in due course.

6.5 Multiple Insured or Potential Beneficiaries

Generally, an insurable interest is required for multiple insureds and beneficiaries who are not named in the contract; mortgagees, for example, do have an interest in the relevant policy through their loan secured on the relevant property. For life policies, the position is a little less straightforward – where there are "mid-term beneficiaries" in multi-life policies, the requirement for an insurable interest at the time the policy is taken out means that, in theory, the policyholder lacks an insurable interest in respect of those potential beneficiaries. The draft bill (see **6.4 Legal Requirements and Distinguishing Features of an Insurance Contract**) contains wording intended to clarify the position in favour of such potential beneficiaries.

6.6 Consumer Contracts or Reinsurance Contracts

Consumer contracts tend to have more protection for the insured through regulation. CIDRA 2012 provides clarity to consumers on what information they need to provide to insurers when taking out an insurance policy. It removes the duty on consumers when buying or renewing insurance to volunteer information, replacing it with a duty to take reasonable care not to make a misrepresentation. Generally, representations will be made by consumers in response to questions raised by the insurer.

In relation to consumer contracts, CIDRA 2012 also requires the insurer's remedies to be proportionate to the failings of the insured. This means that an insured is not unfairly deprived of all cover in circumstances where an insurer would still have accepted the risk had it known the full facts.

7. ALTERNATIVE RISK TRANSFER (ART)

7.1 ART Transactions

The term "alternative risk transfer" encompasses a number of alternative techniques used to transfer risk as compared with traditional contracts of (re)insurance. As such, the type and structure of an ART transaction will affect its regulatory treatment. (Re)insurers in the UK have used ART for a number of years and where the technique used includes some transfer of risk, regulatory credit will be given for that transfer if it meets the specific criteria set out in the Solvency II Regulation. The Solvency II Regulation explicitly recognises risk mitigation techniques used to transfer a variety of risks, including underwriting risk, but only if they fulfil the relevant criteria.

Industry loss warranties (ILWs) are a type of contract that pays out upon the occurrence of a market loss of agreed severity in response to certain catastrophe events. There might also be a double trigger of loss to the insured/reinsured in addition to market loss. There can, however, be considerable basis risk – ie, the risk that whatever loss the (re)insured suffers will not be fully compensated by the ILW recovery because the two do not exactly match or because the market trigger is not reached. They may not therefore attract much Solvency II credit and for

that reason there may be more careful matching of triggers and more payouts based on indemnity rather than fixed-sum payouts.

A new onshore insurance-linked securities (ILS) regime was implemented in the UK with effect from 4 December 2017. The UK regime has been set up to be fully compliant with Solvency II rules on special-purpose vehicles and therefore the appropriate reinsurance credit under Solvency II should be received.

7.2 Foreign ART Transactions

ART transactions from other jurisdictions will be treated as reinsurance for UK cedents if the contract can be shown to fulfil the common law definition of insurance and also fulfils the Solvency II Regulation's requirements for recognition as a risk mitigant. ART transactions structured as derivative contracts can also be recognised as a risk mitigant if they fulfil the conditions for derivatives as risk mitigants.

8. INTERPRETING AN INSURANCE CONTRACT

8.1 Interpretation of Insurance Contracts and Use of Extraneous Evidence

Insurance contracts are construed according to the principles of construction generally applicable to other contracts. The following general rules of construction apply:

- words will be given their ordinary meaning, but will be understood in the context of the contract and not in isolation;
- where words have a technical meaning in law, they will be taken to bear that meaning; if words are defined in the contract, their own definitions will prevail;
- when construing the contract, the court may consider evidence of background circumstances (the factual matrix);
- if words are ambiguous, they will be construed contra proferentem so that any reasonable ambiguity in the wording will be construed in favour of the insured;
- the contract will be construed in accordance with sound commercial principles and good business sense;
- the contract will be construed in a manner that avoids unreasonable results, provided "no violence" is done to the words used; and
- terms may be implied if this is necessary to give business efficacy to the contract; however, no term will be implied unless it is reasonable.

8.2 Warranties

The IA 2015 reformed the law of warranties and remedies for fraudulent claims in relation to consumer and business insureds.

The IA 2015 abolished the "basis of contract" clause in insurance contracts, which turns an insured's representations into warranties. Breaches of warranty that are irrelevant to the loss that occurs will no longer discharge insurers from liability.

Where the insured can demonstrate that a failure to comply with a contractual term, including a warranty, could not have increased the risk of the loss that occurred, insurers will no longer be able to rely on the breach to exclude, limit or discharge their liability. A breach of warranty will discharge the insurer from liability for loss occurring after the breach but not from liability for loss occurring before the breach or after the breach has been remedied.

8.3 Conditions Precedent

Contracting Out of the IA 2015

The IA 2015 provides that breaches of warranty that are irrelevant to the loss that occurs will no longer discharge insurers from liability (see **8.2 Warranties**). In consumer contracts, any attempt to contract out of any part of the IA 2015 will be of no effect. In commercial contracts, an insurer seeking to contract out of the provisions of the IA 2015 must take sufficient steps to bring the relevant term to the insured's attention and ensure that the term is clear and unambiguous as to its effect.

Fraudulent Claims

The IA 2015 enables insurers to treat the insurance contract as terminated from the date of the fraudulent act. The previous common law position of insurers not being liable for fraudulent claims and being able to recover payments made to the insured in respect of a fraudulent claim remains unchanged.

9. INSURANCE DISPUTES

9.1 Insurance Disputes over Coverage

Coverage Disputes

It is common for an insurance contract to specify a mechanism for dealing with disputes prior to resorting to litigation or arbitration. This may range from an initial attempt to resolve the dispute through nominated senior executives or managers to other dispute resolution mechanisms, such as an independent expert determination or mediation. Whilst insurance disputes are often litigated, it is common for commercial insurance contracts and reinsurance contracts to contain an arbitration clause providing for disputes to be settled through arbitration rather than the courts.

Consumer contracts have to contain certain provisions required by law or regulation to protect consumers. Whilst consumer contracts are sometimes litigated, insurers must provide consumers with details of complaints procedures and their right to refer disputes to the financial ombudsman. They are also under a regulatory duty to treat customers fairly. Consumer disputes will therefore often be settled through internal procedures or an ombudsman ruling rather than through the courts.

Limitation Period for Insurance Claims

There is no specific statutory limitation period for making a claim under an insurance or reinsurance contract. Insurance contracts are subject to the normal limitation period under the Limitation Act 1980 for causes of action founded on breach of contract (six years from the date on which the cause of action accrues).

As well as the statutory limitation period, insurance and reinsurance contracts typically include a notification clause requiring the insured to give the insurer notice of claims or losses, or of circumstances that give rise to a claim or loss, in a particular manner (usually in writing) and within a particular period (for example, "as soon as reasonably practicable"). An insured can lose the right to an indemnity for failure to comply with a notification clause where compliance is a condition precedent to bringing the claim. "Claims made" policies provide cover for claims actually made within the policy period – usually a year.

Enforcement of Insurance Contracts by Third Parties

The Contracts (Rights of Third Parties) Act 1999 allows for third-party enforcement in certain circumstances. For example, a third party may be able to enforce a contractual term in an insurance contract if:

- they are specifically mentioned in the contract as someone who has rights under the insurance contract; or

- the insurance contract seeks to confer a benefit on them.

In practice, however, contracts of insurance usually exclude the Contracts (Rights of Third Parties) Act 1999.

9.2 Insurance Disputes over Jurisdiction and Choice of Law

The rules applicable to disputes over jurisdiction regarding civil and commercial matters largely depend on the domicile of the defendant and the date when the proceedings were instituted.

- The European regime will apply (i) where the defendant is domiciled in an EU or European Free Trade Association (EFTA) state or has a specified connection to one of these states and (ii) where the proceedings were initiated in the UK before 31 December 2020. The "European regime" refers to the application of Council Regulation (EC) 44/2001 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters, commonly known as the "2001 Brussels Regulation" (applicable to proceedings instituted before 10 January 2015) and Regulation (EU) No 1215/2012 of the European Parliament and of the Council of 12 December 2012 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters, commonly known as the "Recast Brussels Regulation" (applicable to proceedings instituted after 10 January 2015). It also refers to the 2007 Lugano Convention.
- Common law rules (i) will apply where the defendant is domiciled outside the EU and (ii) will also apply to EU and EFTA-domiciled defendants for proceedings commenced after 31 December 2020, subject to what is said immediately below.
- The Hague Convention on Choice of Court Agreements (2005) (the "Hague Convention" or the "Convention") applies to contracting states of the Convention and requires the court designated in an exclusive jurisdiction agreement (entered into after the Convention came into force) to hear the case, generally preventing courts of other contracting states from hearing parallel proceedings. As the UK joined the 2005 Hague Convention in its own right on 1 January 2021, the view of the European Commission is that the Convention will only apply after that date. The UK, on the other hand, is of the view that it will apply from October 2015, when the UK became a party to the Convention by virtue of its EU membership. The position in this regard has yet to be clarified.

Where the European regime applies, jurisdiction in matters relating to insurance is determined on the basis of distinct reforms in Chapter II, Article 3 of the Recast Brussels Regulation, which aim to protect the so-called weaker party. Article 3 provides an exception to the general rule that a defendant should be sued in the country in which they are domiciled.

Disputes over the law applicable to contracts concluded after 17 December 2009 are resolved on the basis of the rules set out in Regulation (EC) 593/2008 of 17 June 2008 on the law applicable to contractual obligations, commonly known as the "Rome I Regulation" or "Rome I". Unlike the previous European regime set out in the Rome Convention on the Law Applicable to Contractual Obligations 1980 (transposed in the United Kingdom through the Contracts (Applicable Law) Act 1990), Rome I applies to insurance contracts, with the exception of certain life assurance contracts.

Rome I has been incorporated into UK domestic law through UK Rome I, a retained EU Law version of Rome I with minor operational amendments that do not affect the substance of the law. In practice, this means that UK courts will

continue to apply Rome I in respect of contracts entered into prior to 31 December 2020 (ie, the end of the transition period), and UK Rome I to contracts entered into after this date.

9.3 Litigation Process

Civil litigation in England and Wales is adversarial in nature. The first stage in typical court proceedings is the issuance of a claim form, which contains the names of the parties, details of the claim and its value. The claimant then serves the claim form on the defendant, and must also prepare and serve the particulars of the claim, stating the facts on which it relies, the remedy sought, and any other relevant information. Legal argument will usually be reserved for the actual trial.

The defendant can choose to defend against the claim by serving a defence. The claimant can reply to the defence. If the defence includes a counterclaim, the claimant's reply must also include a defence.

Next steps include disclosure, when each party is required to disclose to the other documents within its control that are relevant to the issues in dispute. The disclosure obligation in English litigation is wide and requires each party to disclose documents that support or harm their case or their opponent's case. Parties will also typically exchange witness statements on issues of fact and expert reports.

The case will then proceed to trial. English trials principally involve each party's counsel making oral submissions and drawing the judge's attention to the relevant evidence and law, including calling on the evidence of witnesses and experts upon which they seek to rely, and cross-examining opposing witnesses and experts.

The parties must take each step within prescribed periods of time set out in the civil procedure rules, or decided by the court, including in case management conferences (CMC) where the parties and the judge decide how the case should be conducted, including setting a timetable for all the steps up to trial.

9.4 The Enforcement of Judgments

If an unsuccessful party does not voluntarily comply with the judgment of the court, various enforcement procedures are available, including the seizure and sale of that party's assets or the imposition of a charge over certain assets.

There are four regimes for the enforcement of foreign judgments in the UK, and which regime is applicable will depend on when and where the proceedings were initiated.

- The UK regime – judgments from Scotland or Northern Ireland will follow the UK regime.
- The European regime – judgments from EU and certain EFTA countries will fall under the European regime (which combines provisions contained in the 2001 Brussels Regulation, the Recast Brussels Regulation and the 2007 Lugano Convention) if the judgment was handed down before 31 December 2020. Under the European regime, the judgment creditor requires the leave of the court to enforce a foreign judgment, following which it can be enforced as if it were an English judgment. Enforcement procedure in these cases will still depend on the law of the enforcing state. For judgments issued after 31 December 2020, the statutory regime or the common law rules that apply to the enforcement of judgments from non-EU/EFTA countries will apply instead. So far, the UK's attempts to accede to the Lugano Convention after 31 December 2020 have proved unsuccessful. The only agreement that the UK has reached in this respect to date is the treaty signed with Norway on 13 October 2020, which provides for the continued application of the enforce-

ment provisions of the 2007 Lugano Convention.

- The statutory regime – judgments from most Commonwealth countries and certain other countries covered by statutory instruments such as the Administration of Justice Act 1920 and the Foreign Judgments (Reciprocal Enforcement) Act 1933 are enforced under the statutory regime. Enforcement under the statutory regime requires a registration of the foreign judgment, without the need to commence a fresh action or to issue notice to the debtor until registration is to be ordered. The onus falls on the debtor to apply to set the registration aside.
- The common law regime – judgments from the rest of the world (ie, countries that are not covered by the European regime after 31 December 2020 or by the statutory regime) are enforced under the common law regime, unless they are subject to other arrangements. When enforcement is sought under the common law regime, the judgment debtor needs to commence fresh proceedings to enforce the foreign judgment as a debt. The grounds for resisting the enforcement under the statutory regime and common law regime are wider than under the European regime, and will depend on the country where the judgment was given, since a foreign judgment is only enforceable under the common law regime if the original court had jurisdiction according to the rules that English law applies in such cases.

In addition to the above, if there is an exclusive jurisdiction clause, then the Hague Convention will apply. If the exclusive jurisdiction clause was entered into after 31 December 2020, then the Hague Convention provides for the enforcement of judgments in a similar way to the Recast Brussels Regulation and will apply to the enforcement of judgments from the signatory countries, including the EU member states, Mexico, Singapore and Montenegro. If the exclusive jurisdiction clause was entered into before 31 December 2020, then the situation is currently unclear given the uncertainty of the application of the Hague Convention to exclusive jurisdiction clauses agreed after 1 October 2015 but before the end of the transition period (see **9.2 Insurance Disputes over Jurisdiction and Choice of Law**).

9.5 The Enforcement of Arbitration Clauses

Arbitration clauses in commercial insurance and reinsurance contracts can be enforced in the same way as arbitration clauses in other kinds of contracts. Indeed, arbitration is a popular method of resolving insurance disputes. The Insurance and Reinsurance Arbitration Society (ARIAS (UK)) has prepared a recommended arbitration clause, which takes into account the ARIAS Arbitration Rules and the provisions of the Arbitration Act 1996 (the “1996 Act”).

9.6 The Enforcement of Awards

Under Section 66 of the 1996 Act, arbitral awards can be enforced as a judgment with leave of the court, whether they are domestic or foreign.

The UK is a signatory to the New York Convention, which entered into force on 23 December 1975, with a reciprocity reservation. The UK has submitted notifications extending the territorial application of the New York Convention to Gibraltar, the Isle of Man, Bermuda, the Cayman Islands, Guernsey, Jersey and the British Virgin Islands.

For foreign awards governed by the New York Convention, Section 103 of the 1996 Act contains the grounds of review for recognition and enforcement, which are set out in Article V of the New York Convention. In practice, the UK is an “arbitration-friendly” jurisdiction and the grounds for review of foreign awards are limited.

In addition to the New York Convention, the UK is a party to the Geneva Convention on the Execution of Foreign Arbitral Awards of 1927, the Convention on the Settlement of Investment Disputes between States and Nationals of Other States of 1965 and numerous other bilateral and multilateral investment treaties.

9.7 Alternative Dispute Resolution

Arbitration is commonly used in insurance and reinsurance disputes, and a clause requiring this form of dispute resolution to be used may be contained in the policy. The International Chamber of Commerce (ICC) and the London Court of International Arbitration (LCIA) are frequently used.

A contract might also require resolution of a dispute through another form of alternative dispute resolution, such as mediation. The court will encourage mediation before litigation for insurance and reinsurance contracts, and failure to attempt it may result in costs penalties.

9.8 Penalties for Late Payment of Claims

The Enterprise Act 2016 introduced an implied term to (re)insurance contracts that insurers must pay sums owed to policyholders within a reasonable time. The type of insurance, the size and complexity of the claim, compliance with any relevant statutory or regulatory rules or guidance, or factors outside the (re)insurer's control will be taken into account when assessing what constitutes a reasonable time.

A breach of this implied term could give rise to a claim for damages. The limitation period for the insured to bring the claim for damages is one year from the date of the last payment in respect of the relevant loss (Limitation Act 1980).

Parties to a non-consumer contract can contract out of the reasonable time obligation, provided they comply with the IA 2015 transparency provision.

9.9 Insurers' Rights of Subrogation

As a result of the doctrine of subrogation, an insurer may pursue third parties for claims pursuant to which the insurer may be liable to the insured. The insurer can "step into the shoes" of the insured and pursue in the insured's name or require the insured to pursue claims that may lie against third parties in respect of the insured event giving rise to a claim under the policy. To trigger subrogation, at common law it is necessary for the insured to be fully indemnified as a condition to the insurer exercising its subrogation rights. In practice, the extent of – and circumstances for – the exercise of subrogation and procedures applicable is specified in the policy.

10. INSURTECH

10.1 Insurtech Developments

An increasing number of start-ups are applying new technologies in the insurance space. Incumbent insurers are focused on partnering with and acquiring these businesses in order to avoid disruption, meet evolving customer demands and capitalise on insurtech's potential.

Strategies/Collaboration

Several of the most common strategies are listed below. Importantly, these strategies are not mutually exclusive and global players typically utilise several in parallel, if not all of them.

- Establish incubator – it is common for insurers to establish incubators with the aim of accelerating seed or early-stage technology ventures. Incubators often take the form of external acceleration programmes that admit and train applicants, though they may equally be internal research and development outfits.

- Venture capital investment – these investments are made directly through a business unit or through a standalone venture capital-focused investment fund.
- Partnerships – by allowing incumbent insurers and disruptors to combine resources, partnerships offer potential benefits to incumbents and start-ups.
- Licensing technology – rather than incurring the risk and expense of growing or acquiring technology, insurers may seek to license fully developed technology from third parties.
- M&A – insurers also seek to acquire insurance-oriented technology companies outright and integrate them into their global brand.

Products

Below are some of the products involved in insurtech.

- Artificial intelligence and machine learning (together, AI) – AI promises substantial improvements in operational efficiencies and pricing accuracy. Products in this area vary, from drones analysing crop health from aerial images of farms to companies offering a completely automated claims service.
- Intelligent agents – virtual and digital assistants and chatbots capable of interacting with customers are becoming increasingly common.
- Internet of things (IoT) and big data analytics – IoT refers to the connection of devices to the internet and/or each other. Insurers use data from wearables to project health outcomes, whilst data from automobiles can predict the likelihood of future accidents.
- Blockchain – this is a digital peer-to-peer ledger system designed to securely record transactions in digital assets, and ownership thereof. Global and UK insurers remain focused on the technology, as is evidenced by their near-universal participation in the B3i initiative, which involved launching a (re)insurance contract management platform using distributed ledger technology (DLT) and smart contract technology.

10.2 Regulatory Response

Efforts have been made by regulators to adapt to insurtech, demonstrated by the launch of Project Innovate by the FCA in 2014. A key component of the project is the regulatory sandbox. This involves early, open and honest communication between insurtech firms and their respective regulators, who provide individual guidance, potential modification of rules and letters of no enforcement action for a limited duration. The FCA closely monitors the pilot and receives information regarding current innovations.

11. EMERGING RISKS AND NEW PRODUCTS

11.1 Emerging Risks Affecting the Insurance Market

As a centre for the global (re)insurance industry, the UK industry – particularly Lloyd's and the London market – is focused on the many emerging risks common to those in the rest of the world, including catastrophe and environmental risk from climate change, cybersecurity risk and the changing risk profile of common types of insurance, such as motor and liability, with the development of automation and AI (see also **12. Recent and Forthcoming Legal Developments** in connection with the developments arising from the COVID-19 pandemic).

Climate Change

Climate change has in recent years ranked amongst the top emerging risks identified by the UK and global (re)insurance industry. Experts ranked it as the top risk in 2018 and 2019, although it was displaced by the COVID-19 pandemic in 2020. Given the ongoing impacts to global economies arising from the

effects of climate change, as well as the impact to (re)insurers in respect of the asset and liability side of the balance sheet, it may be unsurprising that climate change remains a key emerging risk affecting the market.

The UK government has indicated its commitment to the green economy and the PRA and FCA have shown that they are aware of the risks facing the industry from climate change. The PRA's 2021 Climate Biennial Exploratory Scenario (CBES) is designed to explore the resilience of the UK financial system to the physical and transitional risks associated with three scenarios of early, late and no additional action. They expect to publish the CBES results in May 2022.

Cyber-Risk

UK businesses have a heightened awareness of the threat that cybercrime poses, following a number of recent high-profile data breaches. The joint report on cyberthreat to UK business from the National Cyber Security Centre (NCSC) and the National Crime Agency (NCA) acknowledged the pace at which cyberthreats evolve, and urged collaboration between government, law enforcement agencies and business to tackle this universal threat. In its Annual Review 2021, the NCSC stated that it had been involved with, or defended the UK from, 777 cyber-attack incidents in the previous 12 months. Whilst (re) insurers face cyber-risks themselves, it is also an opportunity for them to offer cyber-risk insurance protection to others.

The UK government is committed to making the UK a leader in cybersecurity, and the FCA and PRA are alive to the risks that financial services firms such as (re)insurers face from cyberthreats. The PRA and FCA are engaging with industry and co-operating with each other and the Bank of England (BoE) to monitor the use of new technologies, assess emerging regulatory risk and test firms' operational resilience and cyber-resilience through stress tests – and to apply enforcement and fines when regulatory and data breaches occur.

Longevity Risk

Longevity risk has been an increasing focus of the regulator, due in part to the peculiarities of Solvency II. In 2017, the PRA recognised that the design of the risk margin makes it highly sensitive to interest rate conditions. In the BoE's public response to the European Commission's Call for evidence: EU regulatory framework for financial services, the PRA noted that interest rate sensitivity, coupled with historic low rates in the UK, meant that the risk margin is disproportionally large for UK insurers writing interest rate-sensitive risks, which are usually long term. The PRA also noted that the volatility was undesirable from a prudential viewpoint because of its potential to promote pro-cyclical investment behaviour by insurers. Consequently, the PRA publicly supported redesign of the risk margin to deliver more stable balance sheet outcomes for insurers and thereby support their key role as long-term investors in the economy.

In a recent review of Solvency II announced by HM Treasury for the UK post-Brexit, it was indicated that reform to the risk margin was part of the agenda.

11.2 New Products or Alternative Solutions

Blockchain

Several features of DLT, such as blockchain, justify its reputation of offering a high standard of protection against cybersecurity risk. From the sharing of identical information across networks to the cryptography-based protections built into the technology, DLT represents an exciting development in the fight against cybercrime. The ability to protect data from cyber-attacks or malicious tampering is not only beneficial

from a business risk point of view, but it also makes a product based on DLT more attractive to both consumers and regulators, who must balance innovation against risks to markets and customers. However, weaknesses in DLT have been revealed through a series of cyber-attacks against digital currencies that use DLT.

To manage the policy and regulatory implications of DLT and crypto-assets in financial services, in March 2018 the BoE, the FCA and HM Treasury created a Cryptoassets Taskforce, which published a report in October 2018 detailing specific actions to be taken by regulatory authorities to mitigate the risks that come with the potential benefits of DLT. The FCA issued its own guidance on crypto-assets in July 2019 (PS19/22), following a January 2019 consultation, and the PRA issued a Dear CEO letter in June 2018 on exposure to crypto-assets. HM Treasury published a consultation in January 2021 on the UK's regulatory approach to crypto-assets and stablecoins.

12. RECENT AND FORTHCOMING LEGAL DEVELOPMENTS

12.1 Developments Impacting on Insurers or Insurance Products

COVID-19

The impact of the COVID-19 pandemic in 2020 and 2021 has seen above-average major claims activity, particularly with business interruption insurance. The industry has strongly advised the UK and other governments globally to introduce a public-private risk-financing mechanism for future pandemics, referred to as "Pandemic Re", which is modelled off the UK government-backed terrorism risk mutual "Pool Re".

In addition, regulators have taken an active role in approaching the issues posed by COVID-19. In the UK, the FCA initiated a test case on business interruption insurance and, in January 2021, the Supreme Court issued a judgment that substantially allowed the appeals of the regulator. However, there were certain qualifications given to the Supreme Court's findings, meaning that insurers and insureds will need to continue to carefully consider their policy language.

With regard to the issue of causation, rather than following the "but for" test, the Supreme Court determined that where there are multiple concurrent causes of loss, only one of which is covered by the policy, unless the other cause is specifically excluded, the insurer may be liable. However, it remains dependent on the policy wording itself to determine whether this causal connection is sufficient to trigger the insurer's obligations. In addition, as part of its judgment, the Supreme Court overruled the Orient Express case, which is likely to have wider implications for business interruption policies beyond the pandemic. The judgment is also likely to result in potentially difficult discussions between cedants and reinsurers, and, in some cases, may result in litigation over the extent of coverage. The FCA continues to collect and publish data from insurers on their progress with business interruption claims.

Part VII Transfers

In the UK there are specific provisions (in Part VII of FSMA) allowing one insurer to transfer its business to another, without the requirement for policyholder consent or consent from any other affected counterparties (a "Part VII transfer scheme"). There have been a large number of these over the past few years due to M&A activity and reorganisations driven by Solvency II or Brexit. However, it is no longer possible to commence a Part VII transfer to transfer business between a UK authorised firm and a firm authorised in an EEA state.

A judgment of the High Court delivered on 16 August 2019 by Mr Justice Snowden refused to sanction a proposed Part VII transfer scheme whereby Prudential proposed to transfer annuity policies (constituting approximately GBP12.9 billion of liabilities) to Rothesay Life. Upon appeal, the Court of Appeal overturned the refusal to sanction the proposed transfer and the High Court has subsequently approved the transfer.

13. OTHER DEVELOPMENTS IN INSURANCE LAW

13.1 Additional Market Developments

Brexit

The transitional period ended on 31 December 2020. Although a trade agreement was agreed between the UK and the EU, it contains very few provisions on (re)insurance and the UK is now treated as a third country (resulting in a loss of passporting rights between the UK and the rest of the EU). The UK and the EU committed to agreeing a memorandum of understanding (MoU) on a framework for co-operation between financial regulators by March 2021. The MoU is intended to facilitate discussions between the UK and the EU on how to move forward with equivalence determinations.

Although the UK and EU confirmed in March 2021 that a text had been agreed in principle, no MoU has yet been formally agreed or published. The UK has granted a package of equivalence decisions to the EU and EEA member states, including for the three equivalence areas under Solvency II, insurance, group solvency calculation and group supervision. However, as yet, the EU has not reciprocated so the UK has not been granted equivalence under Solvency II.

Insurers have been planning for some time on the basis of a no-deal or hard Brexit to set up new authorised subsidiaries or branches so as to be able to access both the UK and EU markets.

The UK government has drafted legislation intended to maintain EU laws and regulations currently directly applicable in the UK, including those relating to (re)insurance, and in particular Solvency II, but without the references to EU institutions and the reciprocal arrangements that come with being a member, by incorporating these into domestic law through statutory instruments under the European Union Withdrawal Act. The effect is that there is no difference in (re)insurance regulation as it currently applies in the UK and to UK authorised (re)insurers post-Brexit to the regulations that applied immediately prior to Brexit, with the amendments being made purely to reflect the UK's withdrawal from the EU and its institutions.

It is unlikely that the regulators or the UK (re)insurance industry will wish to diverge greatly from Solvency II, given the amount of effort, time and money spent on its implementation. However, changes are likely to be made in areas that are already heavily criticised by the regulators and the industry, notably the risk margin, the matching adjustment and the treatment of certain long-term investments. Each of these was raised in HM Treasury's Call for Evidence on Solvency II, which discussed how Solvency II law and regulation in the UK might change post-Brexit. The UK government has asked the PRA to model different options for change in these areas and a package of reform proposals is expected in the first half of 2022.

In November 2021, HM Treasury published a consultation paper on Future Regulatory Framework Review for financial services which focuses on how the UK's financial services regulation should adapt post-Brexit and provide a greater focus on growth and competitiveness.

Insurance-Linked Securities Regime

The new ILS regime for the UK was implemented after a significant amount of work between the regulators, the industry and HM Treasury to design an onshore regime that would allow the UK to compete with more established ILS jurisdictions, whilst ensuring that ILS issued in the UK would be compliant with Solvency II.

The new rules introduced protected cell companies into the UK for the first time, together with an attractive tax regime and a bespoke approach to regulation and supervision to reflect the nature of ILS transactions. The UK government has launched a tax consultation aiming to make the UK's ILS regime more competitive.

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