Insurance/
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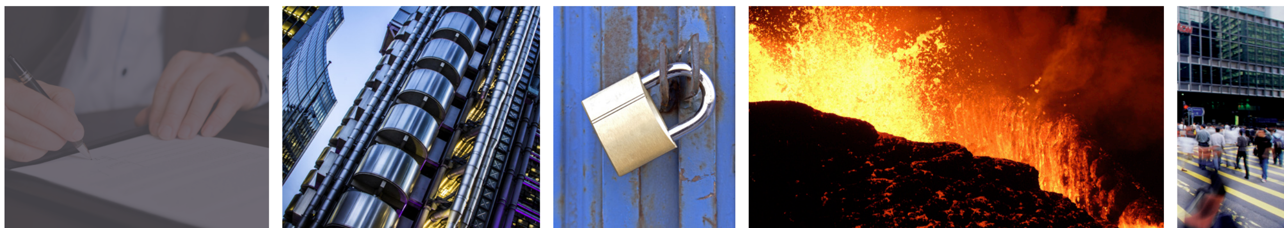

Welcome to HFW's Insurance Bulletin, which is a summary of the key insurance and reinsurance regulatory announcements, market developments, court cases and legislative changes of the week.

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   HFW Partner Andrew Bandurka and Senior Associate Rupert Warren give presentation to LIIBA.

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1. Regulation and legislation

Europe: Brexit – what are the implications for (re)insurers and intermediaries which have passported into or out of the UK?

Although the UK will need to give the EU two years' notice that it is leaving the EU if the "Leave" campaign succeeds in June, (re)insurers and intermediaries which have passported into or out of the UK should already be thinking about the potential impact of a Brexit and how they can deal with the consequences, just as Lloyd's has been doing (see Andrew Spyrou's article – Lloyd's Chairman issues statement to the Insurance market regarding the EU referendum).

The first issue to consider is what the UK's relationship with the EU would look like following a Brexit. The Government has published a paper[1] on the models that the UK could adopt should it leave the EU. The paper outlines three possible types of relationship:

1. The "Norway model" – although the UK would no longer be in the EU, it would remain in the European Economic Area (the EEA). This is the model outside the EU which would be most integrated with the Single Market.
2. A negotiated bilateral agreement – this could involve an advanced bilateral relationship between the UK and the EU, similar to the relationship that Switzerland has with the EU, or could simply be based on a free trade agreement, similar to South Korea's relationship.
3. World Trade Organization (WTO) only membership – if the UK had not agreed a new relationship with the EU by the time it left, the UK's common membership of the WTO would be the basis for trade with the EU, this is the same as Brazil's method of trading with the EU.

The second consideration for members of the insurance sector is the effect on operations on the other side of the UK-EU divide. UK (re)insurers and intermediaries need to consider the impact on their European operations, with European (re)insurers and intermediaries needing to consider their UK operations. One of the main concerns will be whether the current passporting regime will remain, or whether separate approval will be needed to carry on business in the UK (for European entities) or the EU (for UK entities).

1. The Government paper analyses passporting rights and suggests that passporting rights could be maintained only if the "Norway model" was adopted, as passports are available only to firms authorised in EU and EEA states. However, the Norway model would not satisfy the objectives of the Brexit proponents, since the UK would need to maintain open borders with the EU, contribute to the EU budget and accept EU legislative sovereignty.
2. If the UK entered a bilateral relationship with the EU, we anticipate that UK (re)insurers and intermediaries would lose the right to passport throughout the EU, and vice versa, although they might have a right of establishment in the EU if the treaty that was signed gave UK financial services providers the right to create an establishment in an EU country, and vice versa. This relationship would mirror the current agreement with Switzerland, under which EEA insurers have the right of establishment in Switzerland, and vice versa but do not have passporting rights, so need to obtain formal approval from the Swiss regulator. The granting of the right for UK (re)insurers and intermediaries to create an establishment in the EU would probably be contingent on UK insurance regulatory requirements remaining compatible with the equivalent EU requirements. At least initially, this should not be a

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1 https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/504604/Alternatives_to_membership_-_possible_models_for_the_UK_outside_the_EU.pdf

problem, as EU member states have only recently implemented Solvency II, and the Insurance Distribution Directive is due to be implemented by February 2018, before a Brexit could take effect.

3. If the UK relied on its membership of the WTO as the basis for trade with the EU, UK (re)insurers and intermediaries would be unlikely to have even a right of establishment in the EU and European (re)insurers and intermediaries would be unlikely to have a right of establishment in the UK. However, some states which are signatories to the WTO's General Agreements on Trade in Services permit certain types of insurance and/or reinsurance to be sold on a cross-border services basis.

Although Brexit may not come to pass, it is prudent to consider at an early stage how a Brexit could affect operations, and the measures that could be taken to minimise the disruption. There are various options that UK (re)insurers and intermediaries could pursue, such as redomesticating to an EEA state or establishing a subsidiary in an EEA state. EEA (re) insurers and intermediaries would need to consider seeking UK authorisation for a branch or to establish a subsidary in the UK. None of the options could be completed overnight, and in some cases years of planning may be required, e.g. if the redomestication is pursued under the European Company/*Societas Europaea* regime.

We may still be over two years away from the UK severing ties with Europe but it is definitely not too early to start planning for the upheaval that this would bring.

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UK: Lloyd's Chairman issues statement to the Insurance market regarding the EU referendum

John Nelson, the Chairman of Lloyd's, has issued a statement that, following careful consideration, the Council of Lloyd's and its Franchise Board have unanimously concluded that the best outcome upon the forthcoming EU referendum, in the context of the interests of the Lloyd's market, is for the UK to remain a member of the EU.

Notwithstanding this, Nelson explains that the market has been developing contingency plans in the event that the referendum results in the UK leaving the EU so as to ensure that in such circumstances the market can continue to access the EU markets. Nelson says that such access, following Brexit, would become less attractive than the single market access currently enjoyed, and that this change would be inevitable.

The statement followed a speech made in early February about the consequences for Lloyd's of leaving the EU, in which Sean McGovern, Lloyd's Chief Risk Officer, explained that aside from the *"considerable uncertainty"* that such a move would create, not least with regard to the regulatory regime, voting on 23 June 2016 in favour of leaving the EU would *"fuel European financial markets turmoil"* and set a precedent for EU countries to leave the union.

The message has broadcast Lloyd's commitment that, despite the circumstances, they will work towards ensuring business continues to flow to London but will also continue to offer the opportunity to write business in local markets under the Lloyd's structure.

The full message can be read here, and the full speech made by Sean McGovern, Lloyd's Chief Risk Officer, can be found here.

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UK: Third Parties (Rights against Insurers) Act 2010 makes progress – amending Regulations laid before Houses of Parliament

We recently reported[1] on the progress of the Third Parties (Rights against Insurers) Act 2010 (the Act) and our understanding that it would come into force in the "summer"; October at the latest.

On 25 February 2016, the draft Third Parties (Rights against Insurers) Regulations[2] (the Regulations) were laid before both Houses of Parliament. If approved, the Regulations will correct omissions from the Act so that it can, after much delay, be brought into force. The Regulations will extend the circumstances in which the Act applies to include corporate and other bodies which are subject to administration under specified sectoral insolvency regimes or which have been dissolved.

The Minister of State for Civil Justice, Lord Faulks QC, has stated[3] that the Regulations need to be approved by a resolution of each of the House of Commons and the House of Lords and that, following receipt of this approval, the Regulations will be made without delay. Although new regulations can be made at any time during the year, the Government has agreed that new regulations that affect businesses can come into force on only two dates each year, either 6 April or 1 October, known as "common commencement

1 http://www.hfw.com/Insurance-Bulletin-25-February-2016#page_2

2 http://www.legislation.gov.uk/ukdsi/2016/9780111144152/pdfs/ukdsi_9780111144152_en.pdf

3 http://www.parliament.uk/business/publications/written-questions-answers-statements/written-statement/Commons/2016-02-25/HCWS556/

dates"[4]. Common commencement dates prevent businesses being bombarded by new regulations coming into force on numerous dates throughout the year.

Although Lord Faulks QC did not give a commencement date for the Act, he did state that it would not be earlier than three months after the Regulations are made. As Article 1 of the Regulations states that they will come into force immediately after the Act comes into force, it will not be possible for the Regulations to come into force on 6 April 2016. On this basis, it seems that both the Regulations and the Act will come into force on 1 October 2016 ,assuming that the Regulations are approved and made at least three months before 1 October 2016, i.e. no later than 1 July 2016.

We will provide an update when the Regulations are made and when the date on which the Act will come into force has been confirmed.

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4 You can read more about common commencement dates here: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/32233/10-1137-common-commencement-dates-august2010.pdf

2. Court cases and arbitration

France: Supreme Court confirms exclusion of coverage in case of deliberate wrongdoing of the insured

The French Supreme Court, in a decision dated 4 February 2016, upheld an appellate decision which found that an insurer wishing to deny cover by invoking the deliberate wrongdoing of the insured must prove that the insured wilfully breached its obligations.

The decision is interesting as it implies that an insured which acts deliberately in breach of its obligations will not be covered. The French Supreme Court had previously only allowed an insurer to deny cover if it proved not only a wilful breach of its obligations by the insured, but also a clear intention to cause the damage. As a result, a loss resulting from conscious and voluntary misbehaviour of an insured could nonetheless be covered in the absence of intent to cause the inflicted loss. In particular, this meant that professionals who deliberately violate their obligations, not specifically to harm their client, but only to save time or money, could be covered by their liability insurer.

In 2013 and 2014, a few decisions from the Supreme Court suggested a willingness to deprive an insured of cover in cases where it deliberately acted illicitly, with knowledge that this would lead to a loss, even though the primary intention was not to cause the loss itself. However, the Supreme Court had since remained silent on the subject, and it had been speculated that the Court did not wish to confirm this more recent case law.

The decision rendered on 4 February 2016 suggests that the Court has no intention once again to reverse its position. However, since the decision will not be published in the Court's Bulletin, its authority may be questioned. A leading case is therefore still awaited.

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NHS Litigation Authority fails in challenge to recoverability of ATE premium – *Axelrod v University Hospitals of Leicester NHS Trust*

In a judgment handed down in late January of this year in Chester County Court, it was held that a technical challenge to the recoverability of ATE premiums by the NHS Litigation Authority (NHSLA) was unsuccessful. This is not the first time that such a challenge has failed and premium has been held to be recoverable by the Claimant in full.

In *Axelrod v University Hospitals of Leicester NHS Trust*[1], the Claimant, Daniel Axelrod, appealed against a decision at a costs assessment to disallow the recovery of his ATE premium in the value of £5,088. Following the implementation of the Legal Aid, Sentencing and Punishment of Offenders Act 2012, one of the few types of ATE premiums that is still recoverable from unsuccessful opponents is a premium charged to cover the risk that the claimant will be liable to pay for an expert report on liability or causation, provided that certain conditions are met.

Mr Axelrod had undergone surgery at the defendant's hospital, following a fracture in his leg suffered while playing football, during which screws were used to stabilise the fracture. The defendant accepted that one of these screws was too long and caused cartilage damage. In pursuit of damages from the defendant for losses caused by negligence, Mr Axelrod purchased an ATE insurance policy, and the claim was subsequently settled when he accepted a Part 36 offer of £3,000.

However, following provisional assessment that the ATE premium was recoverable by the claimant from the NHSLA, this was challenged by the defendant under the Recovery of Costs Insurance Premiums in Clinical Negligence Proceedings (No2) Regulations 2013 (the Regulations), and on the ground that the premium was disproportionate. Specifically, the defendant argued that the ATE policy failed to state the amount of the recoverable premium in that it did not state what part of the overall premium related to liability to pay for experts' reports, and so did not comply with the statutory regime for recovery. It also argued that the policy did not *"on its face charge a recoverable premium"* because it was not obvious whether or not the sum was a proper premium to charge for the risk of incurring a liability to pay for experts' reports. The defendant submitted that the Court should exercise its discretion to disallow it.

The Judge held that the claimant *"is not limited to recovering the insurance premium only where the policy states the amount of the premium that relates to the risk of incurring liability for expert reports on the issues of liability and causation"* because he did not interpret the Act and its associated Statutory Instruments as requiring such a statement. He therefore allowed the claimant's appeal, with the ATE premium being recoverable in full. On the question of whether the premium was obviously recoverable the Judge stated that while it was unfortunate that the reasonableness of a premium was often difficult to assess, this did not undermine the fact that this was the premium being charged. Its recovery would be subject to the usual rules of costs assessment as to proportionality and reasonableness.

Cases such as this one highlight ongoing concerns that the NHSLA tend to challenge all costs at the conclusion of successful cases. While this judgment does not advocate an excessively strict construction of the legal requirements as to the policy terms, and the Government continues to be lobbied about the wider public policy concern that running such costs disputes is rarely a sensible use of public funds or Court time, ATE insurers of medical negligence claims would be well advised to review policy wordings in order to pre-empt the types of arguments that were raised here.

For more information, please contact Andrew Spyrou, Associate, on +44 20 7264 8789, or andrew.spyrou@hfw.com, or your usual contact at HFW.

1 http://www.litigationfutures.com/wp-content/uploads/Axelrod-ruling.pdf

3. HFW publications and events

HFW Partner Jonathan Bruce gives presentation at Aon CEE mining event

On Wednesday 9 March 2016, HFW Partner Jonathan Bruce gave a presentation at the Aon CEE mining event in Katowice, Poland.

HFW Partner Andrew Bandurka and Senior Associate Rupert Warren give presentation to LIIBA

On Thursday 10 March 2016, HFW Partner Andrew Bandurka and Senior Associate Rupert Warren gave a presentation to LIIBA about business interruption insurance and related E&O hazards.

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