

Politics as Unusual: How do deal with political acts around the world that cause disruption to business activities and impair legal rights

BREXIT SECTION: James Middleton, Associate General Counsel, AIG UK

The outcome of the UK's referendum on EU membership on 23 June 2016 was unexpected, but not unforeseeable. It therefore provides an excellent case study in how businesses can think about their readiness to adapt to political change and a framework for anticipating and reacting to new political circumstances. In the case of Brexit, approaching 4 years on, we still do not really know what the new political landscape will ultimately look like, as no negotiations on the future relationship between the UK and EU have yet taken place. In fact, at the time of writing, we don't even know if Brexit will actually happen and if it does whether it will happen under a managed, orderly transition or a "no deal" crash out (we may know some of the answers to this by the time of the conference but given experience to date, it would be foolish to bet on it!). This section therefore focuses on practical steps to consider when political change is in the air but the direction of the change remains unclear.

1. *Take the time to understand what your organisation relies on in the current political, legal and regulatory framework and what its key exposures are if the anticipated change were to happen.*

In the case of UK insurers wishing to do cross-border business in the other member states, the UK's membership of the EU brings two key benefits:

- (a) Freedom of establishment – the ability to set up and operate from branches of the same insurer in up to 30 other countries, with a single prudential regulator and a single capital pool; and
- (b) Freedom of services – the ability to sell products cross border (subject to complying with local laws in the country of sale).

From the outset, it was clear that the loss of these legal rights for UK insurers operating in the European Economic Area (**EEA**) (and EEA insurers operating in the UK) would necessitate a fundamental corporate restructure in order to establish a separate legal entity in the EEA or UK respectively from which to operate. However by brainstorming with a cross-disciplinary group well ahead of the referendum, it was possible to identify and to begin to plan for, a range of other areas that could be impacted, including:

- data privacy and the ability to make cross border transfers of personal data
- impact on investment portfolios of market volatility
- effects on the labour supply and on existing staff of the loss of the EU freedom to resettle and work in other member states
- recognition of IP rights in the remaining EU countries
- enforceability of judgements by UK courts in the EU and EU member state courts in the UK.
- changes to policy documents
- validity of existing cross border insurance coverage following Brexit
- how resulting economic disruption impacts business planning

... and so on! This process of monitoring and constantly re-evaluating the risks arising from political disruption and their impacts is central to successful management of the change.

2. *Determine your options and contingency plans to mitigate your risks*

UK voters were faced with two choices: Leave or Remain. The meaning of "Remain" was reasonably clear and understood. But the ballot paper did not give any indication of what "Leave" looked like. There were (and at the time of writing, still are) a vast range of outcomes of Brexit,

ranging from a so-called “hard Brexit” where the UK leaves the EU without a deal and with no structure in place for handling the loss of its existing trade and other arrangements with the EU, to a very “soft” Brexit where the UK (along with countries like Iceland, Norway and Liechtenstein) remains a member of the EEA, following 75% of EU rules but not being politically represented in its decision making.

Faced with such a situation, companies need the capability to form their own view on the likely outcomes that they will plan for. In reality though, the only scenario it is possible to prepare for with any real certainty is the “worst case”. By being ready for a worst case scenario, anything “softer” should be easier to handle. In the case of UK insurers wishing to continue doing cross border business, this meant assuming the loss of the freedoms of establishment and service and choosing both a country within the remaining 30 EEA member states to set up their European operations in, and how (from a restructuring perspective) to get there.

A key learning from this experience is the importance of taking on board a broad range of views and perspectives. Everyone comes with their own prejudices and unconscious biases. In a complex political environment, no one person or group has a monopoly of understanding. Only by talking to a broad range of internal and external stakeholders, from different disciplines and geographies, is it really possible to begin informed decision making.

3. *Put yourself in the shoes of your customers and business partners*

Amidst political turmoil, customers in any industry, but particularly insurance, want comfort and reassurance that their provider remains able and ready to meet their needs. AIG prepared a raft of broker and customer communications, ready to go out on the morning of 24 June if the result was “Leave”. Most people thought they would never be used, but it meant our key business partners had a message of reassurance, readiness and stability from us when they arrived at their desks in the midst of an otherwise suddenly very uncertain environment.

4. *Decide whether you want to be a leader or a follower*

The good thing about political disruption is that while some may be affected more than others, typically all industry players have to address it in some way. This gives an opportunity to evaluate whether there is a competitive advantage to be gained in leading the industry response, or whether it is better to “wait and see” the mood of the market before reacting. The danger in being a follower is that in an event like Brexit, under English law, corporate restructurings involving portfolio transfers require court and regulatory approvals and a response could not be left too late in case these bodies became “clogged up” by the rush of approvals needed by firms. Factors like this should be taken account of in decision-making. For AIG Europe, leading the industry in announcing its plans went beyond Brexit – it was also an opportunity to demonstrate our credentials as a front-runner in the market.

5. *Will your contracts still do what you intended them to do in the new political environment?*

Even for those operating in stable political environments, legislative and regulatory change is never far away. All organisations need to remember that their contracts need, wherever possible to be designed to withstand that change. A well-publicised example is the case of the European Medicines Agency which in 2014 took out a 25 year lease in London that it found it could not terminate, despite Brexit (the conditions for the English law doctrine of frustration to apply not having been met). This provides a sobering example of the onus on lawyers to ensure clients are protected as much as possible against even unforeseen political change. Provisions in commercial contracts such as what counts as *force majeure* and material adverse change need to

be thought about carefully by both sides to ensure that the parties are locked in or have an escape route, depending on your commercial objectives.

6. *Capitalise on good corporate governance*

Political disruption is likely to be a high-profile topic and one in which most Boards, Risk and Executive committees will be interested. It is essential to keep these important bodies informed of plans to adapt to political change as circumstances like Brexit are complex and multi-faceted. It would be unreasonable to simply present a full-blown proposal for approval shortly before the implementation deadline. Involving the Board and its relevant committees and taking guidance from them regularly during the process and as the situation develops is likely to lead to a far smoother outcome. Feedback should be incorporated into planning activities and a log maintained of questions raised by the Board and its sub-committees to ensure they are all satisfactorily addressed.

7. *Can your organisation play a role in shaping the change?*

The UK's 45 year+ membership of the EU has shaped almost every aspect of its laws and regulatory framework. Adopting and amending EU law into UK law in readiness for Brexit, at the same time as determining its position on future trade negotiations, has been a gargantuan task for the Civil Service, presenting an opportunity for companies and trade bodies to raise their profiles with government and offer genuine support to help with the overhaul of laws to fit the new political environment. Failure for companies to play their part in this could result in a new landscape which does not take account of their needs: developing a coherent approach to government affairs strategy is a key part of handling any sort of political change.

8. *Is the change actually an opportunity?*

Change is often uncomfortable, especially where enforced by the external political environment. But it is also hard to think of many political changes that have not brought with them some kind of opportunity. AIG, for example, was the first insurer to bring out a "Brexit Addendum" to its D&O policies, providing directors with coverage for certain relocation costs in the event they were forced to move as a result of loss of freedom of movement for UK citizens in EU countries. Brexit provided insurers with a fresh opportunity to re-examine and optimise their European corporate and management structures. Similarly, we are yet to find out how the UK will take advantage of the freedom Brexit gives it to move its own laws and regulations away from those of the EU, but any companies doing business in the UK and/or EU should monitor closely whether such legal and regulatory divergence presents opportunities for innovation in how they serve their customers.

9. *Keep rechecking your plans as the landscape changes*

The British economist John Maynard Keynes famously quipped "When the facts change, I change my mind." In order to create and maintain a competitive advantage, it is essential to be receiving a regular feed of the latest political intelligence and constantly re-evaluating how this affects your plans for adapting to the political change. In the UK this has become a "value added" service that law firms have sought to provide to their clients, with numerous competing "Brexit update" email circulars hitting the inboxes of their in-house brethren every week. Whatever your chosen sources, it is essential to maintain enough flexibility in your planning and approval structures to adjust to new developments or indeed new insights on the impact of the change. The reality is that many of these only come to light after the market has started to implement its plans in sufficient numbers that it is possible to see the side-effects.