IN THE HIGH COURT OF JUSTICE
BUSINESS AND PROPERTY COURTS
OF ENGLAND AND WALES
CHANCERY DIVISION
[2022] EWHC 3161 (Ch)

No. CR-2022-000484

Rolls Building
Fetter Lane
London, EC4A 1NL

Monday 21 November 2022

Before:

MRS JUSTICE JOANNA SMITH

IN THE MATTER OF **USAA LIMITED**

MR S HORAN appeared on behalf of the Applicants.

J U D G M E N T

(v i a M i c r o s o f t T e a m s)

(Please note this transcript has been prepared without access to documentation)

MRS JUSTICE SMITH:

1 This is an application for an order under s.111(1) of Part VII of the Financial Services and Markets Act 2000 ("**FSMA**") sanctioning an insurance business transfer scheme ("**the Scheme**"), together with such ancillary orders pursuant to s.112 of FSMA as the court shall consider necessary or convenient.

2 The application is made jointly by USAA Limited ("**the Transferor**") an English company, USAA S.A. ("**the Transferee**") a Luxembourg company, and USAA S.A. UK Branch ("**UK Branch**") the UK branch of the Transferee which is regarded for financial regulatory purposes as a separate entity and is authorised by the PRA (together "**the Applicants**"). The business being transferred under the Scheme ("**the Transferring Business**") primarily comprises motor insurance provided to members of the US military and their families in the UK and the EEA, together with a small amount of property and general liability insurance. All the Transferring Business is in run-off.

3 The Applicants are indirect wholly owned subsidiaries of United Services Automobile Association ("**USAA**") a Texan company. The Scheme effects a group reorganisation within the USAA group designed to consolidate European business in one Luxembourg entity. Thus, the EEA business and the UK business of the Transferor will be transferred to the Transferee and its UK Branch with the intention that the Transferee becomes the sole carrier of the group's EEA and UK business. It is intended that the Transferor will be wound up once its outstanding liabilities are settled (involving primarily the buyout of UK and German defined benefit pension liabilities) and the PRA agrees to cancel its permissions under Part 4A of FSMA. The transfer is intended to be economically neutral and it is not intended that the parent company will extract any assets as part of the transfer. Assets required to support the technical provisions are being transferred.

4 The primary driving force for the Scheme is Brexit-related, designed to address the fact that as a result of the UK leaving the European Union, the Transferor would no longer be able to benefit from rights derived from the Solvency II Directive (2009/138/EC) ("**Solvency II**") to passport its permissions under Part 4A of FSMA to carry out insurance business in EEA states without having to be authorised in those states. The Transferee started, and the Transferor ceased, writing EEA risks on 1 January 2019.

5 The loss of passporting rights means that a UK insurer is not able to issue new insurance policies across the EEA and may not be able to service existing EEA policyholders or administer claims. It is the potential loss of the Transferor's ability to service policies and to administer claims that the Scheme seeks to avoid. Transferring the policies under the Scheme to the Transferee will provide certainty that there will be continuity of service to the transferring policyholders. It would have been possible for the USAA group to maintain the UK business in the Transferor but it has decided that it would be more cost effective and efficient to conduct its European underwriting through one company and to continue its UK business through a UK Branch of the Transferee. The business will, in fact, be conducted post-transfer by the same individuals as were dealing with it prior to the transfer such that there will be no issue of continuity in terms of administration.

6 The Scheme takes advantage of transitional arrangements set out in the schedule to the Financial Services (Miscellaneous) (Amendment) (EU Exit) Regulations 2019 (SI 2019/710) ("**the Transitional Regulations**") which permit the use of a Part VII FSMA scheme to transfer EEA business where the Scheme was considered to be "in flight" before

the end of the Brexit transition period on 31 December 2020. Any scheme taking advantage of these transitional insurance business transfer provisions needs to be sanctioned by 31 December 2022.

7 I understand from Mr Horan, who appeared on behalf of the Applicants, that the Scheme itself is in a largely conventional form. Many of its provisions are contingent and are unlikely to be operative. There are no unorthodox issues raised by the Scheme, not least because this is a transfer of the whole business. There are provisions for residual assets, which include residual policies, which are unable to be transferred at the Effective Date but will be transferred at a subsequent transfer date. There is similar provision for residual liabilities, which include liabilities attributable to or connected to a residual asset. The Scheme makes provision for residual assets to be held on trust for the Transferee and creates indemnities in favour of the Transferor where transferring liabilities are associated with a residual asset. It is not, however, expected that there will be any residual assets or liabilities. There are provisions for continuity of proceedings by, and against, the Transferor in respect of the Transferring Business to be continued against, or commenced by, the Transferee. The Effective Date of the Scheme is 31 December 2022 at 11.00 pm. UK time. There is provision for the Applicants to agree a later time and date up to 31 March 2022, but it is not expected that that will happen.

8 During the course of his oral submissions today, Mr Horan referred to the case of *Re Phoenix Life Ltd & Ors* [2022] EWHC 1796 (Ch) in which the court gave prospective guidance to the effect that a scheme of the type with which I am concerned does not have to be implemented by 31 December 2022 (i.e. two years from the date of the UK's exit from the EU) provided that the sanction order has been made before the expiry of that period. Given the date of this application, there is no need for me to consider this further.

9 In support of the application, I have received a detailed skeleton argument from Mr Horan which he has helpfully supplemented by way of oral submissions before me today at this remote hearing. I have read two statements from Mr Simon Keith, General Manager and director of the Transferor and also director of the Transferee, dated 19 July 2022 and 15 November 2022, together with a further statement from Mr Simon Baker, a solicitor at the Applicants' solicitors' firm, explaining an error which occurred in the provision of notice to policyholders. I will return to that in a moment. I have also read a report and supplementary report from the independent expert Mr Alex Marcuson ("**the IE**"), Managing Director of Marcuson Consulting Limited, a specialist non-life insurance actuarial consulting firm. The IE's reports conclude that the Scheme does not have any material adverse impacts on affected policyholders or reinsurers. The IE has, I understand, attended the remote hearing in the event of any questions arising and I am most grateful for that.

10 I have been referred to first and second reports from the PRA and the FCA. Neither the PRA nor the FCA, who both have a right to participate in the proceedings under section 110 of FSMA, is formally represented at the hearing, although I understand that a representative of the PRA has attended the remote hearing. No policyholders have objected to the Scheme and no one appears at the hearing to oppose the Scheme. There have been a very small number of representations (amounting to two calls to the helpline and three written responses) but, as I understand it, they do not amount to objections and give no cause for concern.

11 Since the date of Mr Keith's first statement, there has been a small amendment to the Scheme, which he explains in his second statement. However, both the PRA and the FCA have confirmed that they have no comments in respect of the amendment. The IE has

confirmed in his supplemental report that there have been no material changes to the Scheme which change his conclusions.

THE LEGAL FRAMEWORK

12 A scheme will qualify to take advantage of the provisions set out in the Schedule to the Transitional Regulations if, before 31 December 2020 (referred to as the "IP Completion Day", i.e. the end of the implementation period) the relevant fee has been paid to the PRA and the IE has been nominated or appointed (see Schedule para.1). These conditions have been satisfied in this case, as is confirmed by Mr Keith's first statement.

13 The Transitional Regulations alter sections 105, 112, 114, and 114A of Part VII and certain provisions of Schedule 12 of FSMA and the Financial Services and Markets Act 2000 (Control of Business Transfers) (Requirements on Applicants) Regulations 2001 (SI 2001/3625 ("**the Transfer Regulations**") for the purposes of transitional insurance business transfers only. All these provisions were themselves amended on 31 December 2020, but the amendments made by the Transitional Regulations were to the versions of those provisions prior to amendment on 31 December 2020. There is no official consolidated version of the applicable provisions as amended by the Transitional Regulations. However, I was provided with a consolidated version prepared by the Applicants' solicitors, for which I am most grateful.

14 Section 104 of FSMA prohibits insurance business transfer schemes not approved by the court. Section 105(1) defines an insurance business transfer scheme. The Scheme here complies with section 105(1) in that:

(a) It satisfies section 105(2)(a) in that the business to be transferred is part of a business carried on in one or more member states, or the United Kingdom by a UK authorised person (the Transferor) who has permission to effect or carry out contracts of insurance;

(b) It satisfies section 105(1)(b) as the transfer will result in the business transferred being carried on from an establishment of the Transferee in an EEA state or in the United Kingdom; and

(c) The Scheme is not an excluded scheme under sub-sections 105(1)(c) and (3) of FSMA.

15 Section 107 of FSMA sets out the circumstances in which an application may be made to the court. Section 107(2) permits the application to be made by either or both of the transferor concerned and the transferee. The Transferor has its registered office in England while the Transferee does not have its registered or head office in the UK. The application is properly made in England to this court pursuant to section 107(3)(c).

16 Section 108 of FSMA confers upon the Treasury power to impose requirements on applicants making a section 107 application for the sanction of a scheme. The Transfer Regulations, which concern the publication of notices and the provision of notices to relevant parties, were made pursuant to this rule-making power. Under section 108, the court must be satisfied that the Transfer Regulations have been complied with. I shall return to these in a moment.

17 Section 109 of FSMA requires a report from an IE on the terms of the Scheme in a form approved by the appropriate regulator. The IE's appointment and the form of his report has been approved by the PRA.

18 The conditions which must be satisfied before the court may make an order sanctioning an insurance business transfer scheme are set out in section 111 of FSMA. The court must be satisfied that:

(a) The appropriate certificates have been obtained (see Parts 1 and II of Schedule 12) (section 111(2)(a));

(b) The transferee has the authorisation required (if any) to enable the business, or part, which is to be transferred, to be carried on in the place to which it is to be transferred (or will have it before the scheme takes effect) (section 111(2)(b)); and

(c) In the all the circumstances of the case, it is appropriate to sanction the scheme (section 111(3)).

19 Dealing first with the requirements of section 111(2)(a), the PRA states in its second report that there are two certificates required under Schedule 12 of FSMA:

(i) First, a certificate as to margin of solvency under paragraph 2(1)(b). Paragraph 17 of the PRA's second report says this in relation to this certificate:

"The Certificate as to Margin of Solvency certifies that, taking the proposed transfer into account, the Transferee possesses, or will possess before the Scheme takes effect, the necessary margin of solvency. The PRA certifies, pursuant to paragraph 2(1)(b) of Part 1 of Schedule 12 to the Act, that it has received from the authority which it considers to be the authority responsible for supervising persons who effect or carry out contracts of insurance in Luxembourg, certification that, taking the proposed transfer into account, the Transferee possesses, or will possess before the Scheme comes into effect, the necessary margin of solvency applicable to the Transferee. The CAA, as regulator of the Transferee, issues the required Certificate as to Margin of Solvency on 21 July 2022."

A copy of that certificate was attached to the report.

(ii) Second, a certificate under paragraph 3A as to consent by the relevant EEA regulators. Paragraphs 19-21 of the PRA's second report read as follows:

"19. On 29 July 2020 the PRA notified the EEA Regulators of the proposed Scheme. The three-month period (the "**Notification Period**") ended on 29 October 2022 in respect of all EEA Regulators. On 16 November 2022, the PRA issued a certificate in respect of this notification...

20. Of the 8 EEA Regulators consulted for the purposes of the 3A certificate as to Consent, 5 EEA Regulators expressly consented or confirmed they did not object to the transfer by the end of the Notification Period. These were the EEA Regulators in Germany, Greece, Netherlands, Italy, and Portugal.

21. 1 of the EEA Regulators provided no response by the end of the Notification Period. This was the EEA Regulator in Spain.

2 of the EEA Regulators requested further information from the PRA before the end of the Notification Period. The PRA considers that, having provided those regulators with all of the information requested, the presumption of tacit consent also applies. These were the EEA Regulators in France and Belgium. The PRA has included these 2 EEA Regulators in the 3A Certificate of Consent.

22. The PRA is satisfied that no other certificates are required in relation to the proposed Scheme."

20 In his second witness statement, Mr Keith elaborates on the notifications made by the PRA and the responses received, including, in particular, the response from France. The Regulator in France advised the PRA that it published a notice regarding the Scheme in **Journal officiel de la République française** on 25 September 2022 asking interested parties to submit any observations that they may have about the Scheme prior to 25 November 2022 and that it would revert to the PRA after such date to confirm whether it had any objection to the Scheme.

21 At paragraph 61, Mr Keith said this:

"With regards to the response received from:

(a) the regulator in France, I note that:

(i) the Transferor wrote just 781 policies in the jurisdiction between 2019 and 2021 (approximately 1 per cent of the total number of policies written by the Transferor in the UK and the EA during such period);

(ii) as at the date of this witness statement, there are no open claims files in the jurisdiction; and

(iii) the three-month time period in which the French regulator was asked to raise any objections regarding the Scheme has already elapsed."

22 In those circumstances, Mr Keith requested that the court proceed to grant the order on the basis that the French regulator had not objected to the Scheme and he referred to the existence of precedent lending support to that approach.

23 Mr Horan drew my attention in his skeleton argument to two authorities on the issue of tacit consent: *Re Royal London Mutual Insurance Society Ltd* [2019] EWHC 185 (Ch) per Snowden J (as he then was) at [54]-[70]; and *Re Equitable Life Assurance Society* [2019] EWHC 3336 (Ch) per Zacaroli J at [48]-[50]. I am satisfied in light of the PRA report that its certificate complies with the requirements of paragraph 3A of Schedule 12 as explained by Snowdon J in *Re Royal London Mutual Insurance Society*. That is notwithstanding the potential issue raised by Mr Horan as to what the precise certification should be, whether just a certificate from the "home state" regulator or a certificate from the PRA. Here, there are two certificates in any event, as I have already identified. So the point would appear to be academic.

24 As to the requirements of section 111(2)(b) of FSMA, the Transferee has the necessary authorisations required. It is authorised by the CAA, and the UK Branch received authorisation from the PRA on 28 January 2022.

COMMUNICATIONS

25 The issue of publication of notice was addressed by ICC Judge Burton on 25 July 2022 ("**the Directions Order**"). Various orders were made in the Directions Order for publication and also for dispensation pursuant to the Transfer Regulations. Having read the evidence, I am satisfied that this order has been complied with. The publications regime was, in fact, more than was required by the Transfer Regulations.

26 A Communication Pack was sent to all Notified Policyholders and all Notified Claimants as explained in the first statement of Mr Keith. This included a detailed covering letter, a Q&A booklet and the Scheme Summary (including a summary of the IE report). However it erroneously included the Directions Order rather than the formal legal notice in a form approved by the PRA. This has subsequently been explained in the statement of Mr Baker. I am satisfied, in light of that statement, that all of the material information in the notice is contained in the Communication Pack in any event. I accept that there is no detriment to any Notified Policyholder or Notified Claimant and I accept that this omission should not affect the court's discretion to sanction the Scheme.

27 The FCA and the PRA are both content with the way in which communications have been conducted. Neither regulator raises any issue with the omission of the notice from the Communication Pack. The IE reviewed the communication programme in the first IE report and then reviewed its execution in the second IE report. He was satisfied with it and did not raise issue with the omission of the notice.

IS IT APPROPRIATE TO SANCTION THE SCHEME?

28 Having considered the statutory provisions and having read the evidence, I am satisfied that the court has jurisdiction to sanction the Scheme and that all necessary statutory requirements have been met. I turn then to consider, pursuant to section 111(3) of FSMA, whether it is appropriate in all the circumstances of the case to sanction the Scheme.

29 Mr Horan drew my attention to the decision of the Court of Appeal in *Re Prudential Assurance Company Ltd and Rothesay Life PLC* [2020] EWCA Civ 1626, in particular at [75]-[86] which, for present purposes, I need not read out. I summarised the court's discretion in *Re United Kingdom Mutual Steamship Assurance Association Limited* [2021] EWHC 3570 (Ch) at [30].

30 Mr Horan also drew my attention to the fact that a number of decisions have addressed the discretional leeway given to Brexit schemes when weighing up adverse effects against the desire to obtain certainty that policies can be serviced post-Brexit. I note, in particular, the decision of Snowden J (as he then was) in *Re Society of Lloyd's and Lloyd's Insurance Co SA* [2020] EWHC 3266 (Ch) at [70]-[72] and [168].

31 Having read the IE reports in this case with care, together with the reports from the regulators, I accept the evidence that the Scheme will have no material adverse impact on the security of the policyholders concerned.

32 Looking at the IE reports in a little more detail, I note that in the first report, the IE has assessed the financial impact of the transfer on the affected policyholders having regard to the parties' Technical Provisions, their actual 31 December 2021 balance sheets, and their respective projected regulatory capital calculations, together with their financial resources. He has assessed the non-financial impact by looking at how the Transfer will affect matters including the differences in the ways in which the parties are managed and policies are

administered, and changes in the legal and regulatory protections provided to policyholders. He has assessed the impact on reinsurers of the Transferring Policies.

33 At paragraphs 2.3.9-2.3.10 of his first report, the IE said this:

> "In my analysis, I have not sought to compare the position of the EEA Transferring Policyholders post-Transfer with a scenario that could arise if the Transfer did not take place and the Transferor were then unable to continue to administer all of their EEA Business and settle associated claims. The reason for my setting a comparison with this scenario to one side is because:
>
> - it might be possible to conclude that potentially quite disadvantageous arrangements for the Transferring Policyholders post-Transfer were preferable to a situation under which their claims could not lawfully be settled by the Transferor; and
>
> - USAA Staff have told me that were such a scenario to arise, the Transferor would be likely to develop alternative plans to enable them lawfully to continue to administer policies and settle claims for their EEA Business.
>
> Notwithstanding my observation in the previous paragraph, I note that the Transfer is being primarily carried out in response to Brexit and the detriment that would arise to the EEA Transferring Policyholders were it not to proceed."

34 In his first report, the IE raised various issues which he wished to revisit in his second report (albeit at the time of his first report he did not consider that they affected his conclusions as to the Transfer). These included the impact of the Ukrainian/Russian conflict, the effect of the Covid-19 pandemic, the recent increases in price inflation, and changes to foreign exchange rates and climate change risks. In addition, the IE considered what he referred to as key metrics for the Transferor and Transferee assuming a transfer had occurred on 31 December 2021 and showing the likely progression for each of the parties to the ultimate position once the transfer is complete and the Transferor is wound up. Although, in summary, this analysis showed some reductions in the Solvency Ratio for the Affected Policyholders over the period analysed, the IE did not consider that this indicated a material adverse effect arising as a consequence of the Transfer.

35 This led the IE to conclude that, in summary,

- "both of the parties will maintain financial resources well in excess of their regulatory capital requirements both pre- and post- Transfer.

- The Transferring Policyholders will move to a company with a lower Solvency Ratio, albeit not, in my opinion, materially less compared to their position at year end 2021. This change does not arise as a result of the Transfer but as a result of the release of excess financial resources from USAA Limited.

- The Solvency Ratio of the insurer of the Existing Policyholders will ultimately increase relative to its current position. The Transfer will bring about a temporary reduction, however this reflects the injection of excess financial resources into USAA S.A. in anticipation of the Transfer.

36 In his ultimate conclusions, the IE said this:

> "2.13.1. I have concluded that the Transfer will not have a materially adverse impact on the financial position of the Affected Policyholders.
>
> 2.13.2. I have concluded that the Transfer will not have a materially adverse impact on the non-financial position of the Affected Policyholders.
>
> 2.13.3. I have concluded that the Transfer will not have a material impact on reinsurers of the Transferring Polices. I have concluded that the notification and publicity arrangements for the Transfer are appropriate."

37 In his supplemental report, the IE notes that he has reviewed a set of updated projections of the balance sheet of the parties as at the year end 2022 and that he has satisfied himself that there are no changes to any of his conclusions relating to the financial impact of the Transfer. He also notes that he has updated some of his analysis to test the resilience of the parties to scenarios involving higher levels of inflation in the UK and Europe in light of what is now a more uncertain outlook. His conclusion, however, remains the same.

38 He says this:

> "Allowing for all of these elements in the updated financial projections, both of the parties continue to have financial resources that are significantly greater than their regulatory capital requirements, albeit slightly reduced from the levels indicated in my Report. As a result, I am satisfied that the updated financial projections do not cause me to change any of my conclusions regarding the Transfer."

39 The IE did not draw attention to any other material changes in his supplemental report, despite revisiting the various issues that he had identified in his first report.

40 The PRA confirms that it is not aware of any issue that would cause it to object to the Scheme and, accordingly, it does not object to the Scheme. The FCA confirms that it is satisfied that the Scheme is within the range of reasonable and fair schemes available to the Transferor and Transferee and, accordingly, does not object to it.

41 During the hearing, Mr Horan confirmed that there were no issues with foreign recognition, liaisons having taken place with specified regulators in EEA countries, and no issue with policyholder protection schemes and complaint schemes, both of which are dealt with in the IE's report.

42 Having regard to the balancing exercise identified by Snowden J in *Re Society of Lloyd's* at [168], I consider that this Scheme is an entirely appropriate response to the uncertainties created by Brexit, which is unlikely to cause material prejudice to any interested party. It will clearly be far preferable for the EEA business to achieve the certainty that the Scheme provides and no adverse impact has been identified for the UK business.

43 In all the circumstances, I will sanction the Scheme and make appropriate ancillary orders.

CERTIFICATE

Opus 2 International Limited hereby certifies that the above is an accurate and complete record of the Judgment or part thereof.

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Official Court Reporters and Audio Transcribers
5 New Street Square, London, EC4A 3BF
Tel: 020 7831 5627 Fax: 020 7831 7737
civil@opus2.digital

This transcript has been approved by the Judge.