Aon plc

'The B of the Bang'

What the UK Government's white paper on Brexit means for business

Risk. Reinsurance. Human Resources.

Empower Results®

Analysing The United Kingdom's exit from and new partnership with the European Union and its implications for people and businesses in the UK, Europe and globally.

With the triggering of Article 50, the UK has entered a period of profound change. Its future relationship with the EU is open to negotiation and its position in the wider world reassessed.
The UK faces considerable uncertainty, with both opportunities and pitfalls evident in the coming years, and business must prepare for significant change as the UK seeks to forge anew its global economic and political position post-Brexit.

To help clients better understand what this may mean for their business, Aon experts have analysed the recent Government white paper regarding Brexit and sought to provide answers to some of the key issues raised in the document.

Scotland has indicated that it wants to remain in the European Economic Area (EEA) in its paper Scotland's Place in Europe, but it appears likely that the UK will exit the EEA. What are the implications for business of a 'grand split' and what might happen if parts of the UK – such as Scotland and London – sought to maintain access?

Mike Van Slooten
Head of Market Analysis, International

Changes to the flow of capital

Despite the currently predicted end to the UK's membership of the European Economic Area, there appears to be little appetite to impede the free flow of capital at this point in time. Both Europe and the UK recognise its importance, with each side seemingly equally invested in maintaining unfettered access. The alternative – one that would see barriers imposed – would not be in their mutual interest and the hope is that a compromise will be reached that will see the continued free flow of capital in Europe.

> *"Free movement of capital means there is nothing to stop insurers and businesses shifting capital to alternative hubs in Europe now, to maintain access to EEA business post-Brexit."*

London's pre-eminent position as a financial centre within Europe, reinforced by its standing on the global stage, should help to maintain the status quo. Over 75% of the capital market business of the other 27 members of the European Union (EU) is conducted through the UK. The UK industry manages £1.2 trillion of pension and other assets on behalf of European clients. The UK is also responsible for 37% of all European IPOs, while receiving more than one-third of all venture capital invested in the EU[1].

Of course free movement of capital means there is nothing to stop insurers and businesses shifting capital to alternative hubs in Europe now, to maintain access to EEA business post-Brexit. Interestingly, the Irish Insurance Regulator has indicated that discussions have already taken place with a majority of the UK's larger insurers who are focused on this course of action.

That said, market access is not a one-way street. In the case of insurance, there are more than 500 general insurance companies headquartered in continental Europe that currently passport into the UK[2]. Processing the expected number of applications for new entities from UK and European insurers is likely to prove a significant headache for national regulators, who are already struggling under the burden of Solvency II.

---

1 Source: The United Kingdom's exit from and new partnership with the European Union
2 Source: Ibid

The UK Government said: 'The public must have confidence in our ability to control immigration. It is simply not possible to control immigration overall when there is unlimited free movement of people to the UK from the EU.' What impact will immigration controls have on attracting and retaining talent?

Matthew Lawrence
Chief Broking Officer, Health and Benefits, EMEA

The anticipated pressure on employee health

If the free movement of workers is lost, there could be knock-on issues for employers to address in the context of employee health, for example.

Recruitment into the National Health Service (NHS) is an ongoing challenge and currently 5% of the NHS workforce (around 57,000) is made up of EU nationals. The status of these EU citizens may come under threat, and in particular their ability to stay in the UK long-term. This means that the NHS will be unable to tap into this migrant labour market, which will challenge its ability to meet future skills requirements and resourcing needs.

Increased pressures in finding skilled labour could have a knock-on effect within the NHS, potentially resulting in problems accessing treatment, concerns around quality of treatment and adding to ongoing budgetary issues. All of this could result in a challenge that employers themselves are forced to address. If employees needing healthcare – from basic treatment to something more specialist - are unable to access treatment promptly, what responsibility falls back on the employer, if any, and by the same token, what demand will be created for alternative healthcare provision?

> *"The use of technology in health management whether this be through health apps or the use of artificial or online mental health support services, are all options the employer should consider"*

The role of private provision of healthcare (in various guises) may increase and this is a good opportunity for employers to consider the options available. Such options range from providing employees with access to services such as GPs or occupational health schemes, through to health-related insurance. These services could be fully funded by the employer, implemented on a shared funding basis or on a pay-as-you-go model, but with the focus being on employees being able to access the right type of treatment, quickly. From an employer perspective this should improve the productivity of their workforce, help people stay in work, return to work quicker, or give them the longer-term support they might require.

Employers could also take the lead in terms of thinking about their current models of engaging employees around health, wellbeing and benefits. The use of technology in health management, whether this be through health apps, the use of artificial intelligence to help give basic guidance on medical conditions or online mental health support services, are all options the employer should consider utilising in an environment where accessing treatment and support is difficult.

The UK Government said: ‘We will not be seeking membership of the Single Market, but will pursue instead a new strategic partnership with the EU, including an ambitious and comprehensive Free Trade Agreement and a new customs agreement’
What form do you think this agreement will take and how will it impact businesses?

Stuart Lawson
CEO of Aon Credit International, EMEA

Negotiating a new trading relationship with Europe

Business in both the EU and the UK will be impacted by the UK’s exit from the Single Market, although the impacts will fall asymmetrically on the UK, even though the EU will be losing one of its largest economies. The UK exports 44% of its goods to the EU (the EU is the UK’s largest export market) whereas the EU exports just 7% of its products to the UK. This could have an influence on the negotiations that take place.

> *“It may be the case that the UK will base negotiations on a sector basis to minimise the impact on key industries”*

The way competitive multinational, businesses operate currently involves complex supply chains, with buyers and sellers based in different countries. Many UK businesses will have operations in a number of European countries to maximise access to expertise, and maintain cost efficiencies. It will be imperative for goods to remain able to move freely across borders without burdensome customs declarations, and tariffs or controls to minimise disruption. It may be the case that the UK will base negotiations on a sector basis to minimise the impact on key industries.

Although it is not certain how the free trade agreement the government want to negotiate will look, it is certain that UK based firms will have to consider carefully what the changes could mean for their business. They will need to be ready to adapt, and start to future-proof themselves for any possible impacts.

The UK Government said: 'The [EU] Free Movement Directive will no longer apply and the migration of EU nationals will be subject to UK law.'
What effect will a restriction of free movement have on business and talent?

Matthew Lawrence
Chief Broking Officer, Health and Benefits, EMEA

Restrictions on internationally mobile employees

European Economic Area (EEA) countries are subject to the EU Social Security Coordination Directive. The rules of this Directive apply to people in a number of situations including those who live in one EEA country, but work in another. The way the UK applies these rules means that an individual only pays social security contributions in one country.

"The ability for UK citizens working in an EEA country to access the local healthcare system of that country may be restricted"

When the UK exits the EU, it will no longer be part of this directive, which could result in some internationally mobile employees being subject to double social security contributions - both in the UK and in the EEA country in which they work. Importantly, employers also need to be aware this equally applies in reverse. Employers will therefore need to be aware of the practicalities of this issue, from a contract of employment or a salary and payroll perspective.

Furthermore, the ability for UK citizens working in an EEA country to access the local healthcare system of that country may be restricted. Again, this would also apply in the reverse scenario. It is essential therefore that from a provision of healthcare perspective employers have a clear strategy in place for a new population of employees who, having previously benefitted from this legislation, may now need to be supported in the same way as other internationally mobile employees, including having an approach in place for how they can access local healthcare systems. Moreover, carrier selection will become even more important as providing a compliant policy and a policy with high-quality health benefits and services will be vital.

The UK Government said: 'The European Commission is able to recognise data protection standards in third countries as being essentially equivalent to those in the EU, meaning that EU companies are able to transfer data to those countries freely. As we leave the EU we will seek to maintain the stability of data transfer between EU member states and the UK" Is there a heightened cyber risk associated with leaving the EU?

Renette Pretorius
Cyber Team Leader, Global Broking Centre

The impact of EU cyber regulation on the UK

The EU General Data Protection Regulation (GDPR) which was adopted on the 27th of April 2016, comes into force on the 25th of May 2018 and will repeal and replace the Data Protection Act 1998 in the UK.

The UK will likely comply with this regulation, firstly because the GDPR becomes law before it leaves the EU, and secondly because continued future trade with the EU single market will require that the UK demonstrates an appropriate level of protection for the personal data of European Economic Area (EEA) data subjects.

> *"In an environment in which organisational strategies increasingly include reliance on outsourced service partners, cloud services, mobile technologies and digitalisation, it is increasingly important to develop strategies to address the impact of GDPR on your business"*

When Article 50 of the Lisbon Treaty is triggered on 29th March 2017, it will formally begin the UK's separation from the EU. Separation negotiations will span at least two years and all EU laws will apply to the UK during the negotiation period.

The General Data Protection Regulation (GDPR) applies to all businesses that process personal data in the European Economic Area (EEA) , irrespective of whether the business is located in the EEA, or not. The GDPR will provide enhanced rights for data subjects, add obligations for data controllers and processors, and will introduce a new cross-border regulatory regime with stronger enforcement powers.

Regardless of the outcomes of the exit negotiations between the UK and EU, UK companies that offer goods and services to European customers - or those that monitor the behaviours of citizens residing in the EEA - should continue to prepare for compliance with the GDPR.

In an environment in which organisational strategies increasingly include reliance on outsourced service partners, cloud services, mobile technologies and digitalisation, it is increasingly important to develop strategies to address the impact of GDPR on your business. This includes incorporating GDPR requirements into enterprise risk management and business continuity management planning, as well as documenting GDPR compliance efforts.

The UK Government said: ‘After we have left the EU, we want to ensure that we can take advantage of the opportunity to negotiate our own preferential trade agreements around the world. We will not be bound by the EU’s Common External Tariff or participate in the Common Commercial Policy. But we do want to ensure that cross-border trade with the EU is as frictionless and seamless as possible.”
What difference will leaving the EU make to the potential trade agreements the UK can negotiate globally?

Stuart Lawson
CEO of Aon Credit International, EMEA

In pursuit of global trade deals

Leaving the EU will allow the UK to have greater potential to trade with the rest of the world. The UK has a history as being a global trading nation and will hopefully build on this. From a poll conducted with Aon clients at our Insight Event in November, 2016, 39% of attendees believed that trade with the rest of the world was the greatest opportunity the UK would gain as a result of leaving the EU. The government needs to invest in trade negotiations to allow tariff-free access to the fastest growing, most dynamic export markets in the world.

However, we must remember that this does not mean businesses automatically start to export if they don’t currently. It will be great to have trade deals with the rest of the world, but it’s not going to create any benefit without more companies taking advantage of them. At this moment in time, many businesses are reluctant to take on new markets because of their understanding of opportunities and attitude to risk. Successful companies have traditionally used export credit insurance to lay off the credit and political risks of expansion overseas.

" One conclusion that can be drawn is that by leaving the EU, UK businesses are going to face a shakeup. By refocusing, working out options, and being smart when choosing countries to trade with, they will be prepared for the post-Brexit environment"

Although we have the ability to negotiate our own trade agreements around the world, this is potentially going to be difficult since, away from the single market, we will have reduced bargaining power. It should also be remembered that, as part of the EU, we currently have the ability to access the market access database, which is a great resource for understanding where products will have tariff-free entry. This will need replacing as soon as we leave the EU.

The immediate impact of the Brexit vote was the impact on the exchange rate. For several months now, exports have been able to take advantage, but import costs are now rising so the benefit of the pound is levelling off. On the other hand, the UK is an attractive destination for inward investment.

Exporters need to be quick off the mark in finding opportunities and should be expecting and prepared for trade patterns to change. One conclusion that can be drawn is that by leaving the EU, UK businesses are going to face a shakeup. By refocusing, working out options, and being smart when choosing countries to trade with, they will be prepared for the post-Brexit environment.

Aon clients are increasing their use of credit risk protection (including trade credit insurance), establishing where cover is available and using their policy as a tool to assist entry into new trading territories. UK businesses are inevitably going to be impacted; but being prepared to manage the inherent credit risks will be a key factor to success.

The UK Government said: ‘We are committed to maintaining our status as a global leader on workers’ rights and will make sure legal protection for workers keeps pace with the changing labour market.’
What might be the implication if UK workers’ rights fall out of step with those in the EU?

Matthew Lawrence
Chief Broking Officer, Health and Benefits, EMEA

Shifting dynamics in employment law

The impact of Brexit on employment law and how this potentially impacts employee benefits is an area that requires close attention. There is the possibility that as part of the Brexit negotiations the Government could look to amend some EU-derived employment law, subject to obtaining approval from parliament and having the appetite to do so. That said, much of our employment legislation is already embedded within UK law and the fact that the implementation of some aspects of EU law, such as the Working Time Directive, has seen the UK Government enhance the minimum requirement and increase the paid annual leave entitlement to 28 days including bank holidays for full-time employees.

"As the Brexit process evolves, having a formal and robust governance framework in place is something we would strongly advocate"

The employee benefits space has been either directly or indirectly impacted by EU Directives or Court of Justice of the European Union rulings over the years. More recent examples include rulings relating to holiday pay and employees who are absent from work due to long-term illness, the Employment Equality (Age) Regulations and the EU Gender Directive. In response to these rulings or directives, employers have had to ensure that their benefit programmes and indeed the benefit promises in contracts of employments or other literature, are up to date. As the Brexit process evolves, having a formal and robust governance framework in place, which would include regular reviews of relevant employment law matters and the impact on an employer’s employee benefits strategy and programme design going forward, is something we would strongly advocate.

The UK Government said: 'As the UK leaves the EU, we will seek to establish strong cooperative oversight arrangements with the EU and will continue to support and implement international standards to continue to safely serve the UK, European and global economy"
How will the regulation of UK financial services change once we leave the EU?

Richard Ferris
Chief Counsel, Aon Risk EMEA

Will commercial interests trump political divergence?

This is something that is likely to change over time, and both UK and EU firms will have to remain vigilant to ensure they maintain compliant trading standards in their respective businesses.

While we cannot predict what formal arrangements may emerge from the negotiations between the UK and EU regarding the transaction of financial services and expertise between them, there is a working assumption that all parties will still want, and need, to maintain the integrity of those valuable relationships that exist today. This seems likely to create a tendency to a degree of alignment between UK and EU regulation in a variety of areas.

Put simply, if the EU is a key, or dominant trading partner for a given sector of British industry, then the desire to retain aligned regulation that maintains compatibility between UK and trading requirements and environments, and so eases the cost and complexity of trade, will be strong. This is a substantial factor for the EU-UK relationship, where years of shared legislation has created what may be uniquely similar regulatory macro-environments, even allowing for the sometimes substantial differences in local implementation of EU Directives.

"Political and commercial temptation to seek fiscal advantage in changing given regulations cannot be ignored"

There will inevitably be forces acting against this. For example, the temptation to weigh up the pros and cons of greater or lesser rigour in certain regulatory areas, driven by the pressure to consider what might make certain UK industries attractive to more global, as opposed to European, markets. While this is a dynamic that already exists to a greater or lesser degree between Britain, Europe and the rest of the world, once freed of the existing direct Treaty obligations, both political and commercial temptation to seek fiscal advantage in changing given regulations cannot be ignored as a potential a factor, unless expressly bounded in given areas by detailed and substantive EU-UK trade agreements.

Lastly, geopolitical forces will continue to have an effect. It remains to be seen the extent to which this will divide or unite EU and UK interests, and thus add to or subtract from both aligning and differentiating tendencies across a variety of areas, including regulation.

In one sense the rules of engagement will not change – commerce will still need to maintain a deep and embedded understanding of the regulatory environment to which each industry is exposed, and act accordingly. However, while existing parities will make this simpler on Day One of a legally separate EU and UK dynamic, and commercial laws of attraction will act to preserve alignment, the same forces will also work to introduce entropy and change. Companies at every level of complexity whose trade crosses EU borders will need to remain alert and aware of the changes this may cause.

About Aon

Aon plc (NYSE:AON) is a leading global provider of risk management, insurance brokerage and reinsurance brokerage, and human resources solutions and outsourcing services. Through its more than 72,000 colleagues worldwide, Aon unites to empower results for clients in over 120 countries via innovative risk and people solutions. For further information on our capabilities and to learn how we empower results for clients, please visit: http://aon.mediaroom.com

Aon UK Limited is authorised and regulated by the Financial Conduct Authority

aon.com

FP: GBCXT0002