

SESSION B

GENERAL INSURANCE CONVENTION 1991

LLANDRINDOD WELLS 23-26 OCTOBER

EUROPE

GENERAL INSURANCE STUDY GROUP

Report of the Working Party
on Europe

October 1991

Members

W.M. Abbott
P.J. Akers
R.B. Akhurst
B.R.P. Joseph
K.P.W. Larner
E.J. Levay
M.R. Moliver
K.M. Moyle (Chairman)
G.C. Orros
M.H. Tripp

C O N T E N T S

	<u>PAGE</u>
(1) Introduction	1
(2) European Committees of the Institute	2
(3) The Diplomas Directive	4
(4) Supervision and Forum Shopping	8
(5) Distribution	10
(6) The Effect of European Community Competition Law on Insurance	13
(7) EC Third Non-Life Insurance Framework Directive	16
(8) Insurance Accounts Directive - Non-Life Aspects	23

Appendices

1.	Distribution Patterns in EC States	
2.	Single Market Insurance Legislation	
3.	Forum Shopping	
4.	Third Council Directive)
) see
5.	Annual Accounts and Consolidated Accounts Directive) separate
) document

1. INTRODUCTION

1992 and the Single European Market have been described as the most important development for the UK Insurance Industry this century. The process of convergence began over two decades ago and, in view of the complexity of the practical problems involved, very significant progress towards convergence has been made. Step by step pieces of the jigsaw are being positioned and a consensus is being secured which takes the European Community a few steps nearer to realising the ultimate goal of a truly open European market for general insurance business.

The work of the working party on Europe for GISG last year concentrated on the two major aspects which were felt, at the time, to be of particular interest to actuaries, namely:-

- o the implications of recent major Directives affecting, or likely to affect, non-life insurance and non-life actuarial practice; and
- o a comparative study of current actuarial aspects of European markets and practices, involving extensive overseas research.

It was decided, last year that it would be appropriate for the working parties endeavours to continue. The Framework Directive and the Accounts Directive have, at the time of writing, still not completed the process of Community review to which they are being subjected. However, it has been possible for the working party to comment upon the latest drafts, identifying some of the issues which arise for general insurance actuaries.

It was thought that many of the issues behind the Framework Directive could be identified by conducting a study into "forum shopping". It was found that the number and complexity of issues arising made significant change in the short term unlikely but the issues would be very real for a new venture (perhaps for a European bank moving into insurance) or for American or Japanese entrants.

Given the changes which have been occurring across Europe in the distribution of Life and Pensions products and the appalling results of many carriers, it is perhaps surprising that the changes in distribution of general insurance products has been relatively modest to-date. An attempt has been made to identify the emerging trends across the community for the distribution of personal lines general insurance products: the working party look forward to hearing more about these trends from overseas delegates to the conference or from those UK actuaries with overseas experience.

2. EUROPEAN COMMITTEES OF THE INSTITUTE

The European activities of the Institute are covered by a number of committees. Those which are of particular relevance to general insurance are:

2.1 General Insurance Joint Committee (GIJC)

This Committee is chaired by Terry Clarke and covers all aspects of non-life activity on a joint basis with the Faculty.

2.1.1 It is assisted in its work by a number of working parties and sub-committees; in particular it set up in 1990 a small working party chaired by Ron Akhurst to assist with European aspects including the drafting of responses to consultative documents on European Directives and ensuring that matters of European significance are discussed at the GIJC.

2.1.2 GIJC now also has full responsibility for the General Insurance Study Group (GISG) and its many and varied activities. The GISG sets up ad hoc working parties including for the last two years, one on Europe (now chaired by Keith Moyle) which has taken as its brief the provision of information on Europe and European developments to GISG members.

2.2 European Joint Committee (EJC)

This is chaired by Duncan Ferguson, with the brief of ensuring that all European aspects are fully covered either by the EJC itself or by the other relevant joint committees. The GIJC European Working Party also has a dotted line of reporting to this Committee for general insurance matters.

2.3 Membership Committee

This is chaired by Howard Webb and is responsible for all membership matters, particularly those arising out of the Diplomas Directive and the Groupe Consultatif Agreement and for dealing with applications for Affiliate Membership.

2.4 Education Joint Committee

This is chaired by Bill Stewart of the Faculty and, together with the Director of Education and other specialist committees, is responsible for education strategy, including general insurance aspects.

2.5 Groupe Consultatif

This is the European forum of the individual actuarial associations of the Community countries and is currently chaired by John Martin (to be followed by Carla Angela from Italy). The Groupe has been increasingly influential in Brussels and in 1986 adopted an objective of achieving a formal role for actuaries in non-life business in Europe. It will shortly be considering a proposal for common basis guidance notes for actuaries within the European Community. The Institute and Faculty are both separately represented within the Groupe.

3. THE DIPLOMAS DIRECTIVE

3.1 Background

Freedom to work anywhere in the Community is one of the basic rights laid down by the Treaty of Rome. For professionals, however, this right has been restricted by Member States not generally recognising qualifications gained in other Member States. Professionals wishing to move to another Member State have therefore usually had to requalify before they can practise.

3.2 Sectoral Directives

A number of specialised directives have been agreed which make it easier for members of particular professions to practise throughout the Community. Those affected are doctors, nurses responsible for general care, midwives, vets, pharmacists and architects.

3.3 The General Directive

- 3.3.1 Agreeing these sectoral directives proved to be difficult and slow. Consequently, following a proposal from the Commission, the Council of Ministers adopted a General Directive which applies to a wide range of professions with the intention of making it easier for professionals to work in Member States other than their own. This Directive should have been implemented by each Member State by 4 January 1991, although some countries are notoriously bad at achieving such deadlines. To-date, it is believed that only the UK, Ireland and Germany have implemented the Directive although it is now in effect Community Law.
- 3.3.2 The General Directive applies to any profession regulated in some way by a Member State and for which at least three years' education and training at university or equivalent level is required. It includes professions which are regulated by chartered professional bodies and therefore includes actuaries, accountants, lawyers etc.
- 3.3.3 All professionals, whose qualifications fall within its scope, now have a right to have their qualifications recognised in another Member State. Where the education and training they have received is substantially the same as that in the Member State to which they are going (the 'host' Member State), their qualifications are to be recognised as equivalent.

Where, on the other hand, their education and training differ substantially from that required for the same profession by the host Member State, as is usually the case for actuaries, the applicant has a choice between either an aptitude test (designed to assess their ability to pursue that profession in the host Member State) or a period of supervised practice not exceeding three years.

3.4 The UK Position

The Institute of Actuaries requested the UK Government to seek derogation under the Directive to establish the right of the designated UK authority to choose whether an aptitude test or a period of supervised practice of at most three years would be required, rather than leave the choice to the foreign professional. This request was not granted, so the Institute is bound by the terms of the General Directive.

3.5 The Groupe Consultatif Initiative

3.5.1 The Groupe Consultatif has now achieved agreement, effective from April 1991, to establish a basis, within the terms of the Directive, for mutual recognition of members of other European Community Associations. This recognition to be subject at most to either an assessment of knowledge of local commercial practice or to a period of adaptation of no more than one year. All member associations have agreed this basis, although the Italian associations are at present prohibited by law from admitting anyone but Italians to the roll of Italian Actuaries.

3.5.2 The terms of the agreement also require members of one association wishing to practice formally or regularly in another country to join that country's actuarial association, after fulfilling any necessary qualifying conditions, as full local members. It is considered fundamental to the success of these arrangements that broadly common codes of conduct are in force in each country, even if this necessitates an extension to the role of the local professional associations and this is now under active discussion. Of particular interest will be the definitions of 'regular' practice and of the procedures to be followed by the applicants in each country, including the UK, once these are established.

3.6 Some Issues Arising from the Directive

- 3.6.1 Movement of professionals, including actuaries, around Europe is inevitably going to increase, with the UK having the largest group of actuaries in the Community. While control of 'approved' or 'appointed' actuaries may remain for local statutory purposes (if somewhat constrained by the Diplomas Directive's new freedoms) the Directive will doubtless facilitate and encourage a number of actuaries to widen or even move their geographical field of activity. While opening up some fairly restrictive national practices, it might, however, perversely limit the current relatively unrestricted degree of freedom of operation in other countries where very few controls currently exist.
- 3.6.2 Several of the Insurance Directives refer to actuaries and actuarial work without defining them, for example, The Insurance Accounts Directive. It is left to Member States to produce their own definitions of the work. Currently there are few statutory roles for actuaries in general insurance and clear definitions may, indeed, reduce the freedoms currently enjoyed. Are UK actuaries currently restricted in any practical sense?
- 3.6.3 There are signs of concern in the profession, about the potential for devaluing the UK status of actuaries, but are these pure prejudice? It is clear from conversations with overseas actuaries that they too have comparable concerns. Continental actuaries in some countries are concerned that the UK profession is bigger and more organised than elsewhere in Europe. A legitimate UK concern is that UK actuaries are bound by their profession not to provide actuarial advice where they feel they are not competent, while other bodies often do not have a formal structure and no formal guidance notes. The Groupe Consultatif continues to play an extremely important role in focusing attention on the enhancement of actuarial status generally rather than on divisive national interests.
- 3.6.4 There are clearly overriding practical issues which face any professional working in a foreign country, including language and cultural understanding, the different legal, accounting and administrative frameworks and practices. These issues are faced equally by consultants and in-house actuaries. The Institute guidance on Professional Conduct says that where a member is practising outside the UK there are

some agreements to replace the Institute's guidance with those of the local actuarial body. Usually the agreements are restricted to actuaries who are members of both bodies. The list of agreements is short, namely within North America, including the US and Canadian bodies, Australia, South Africa and India. European developments are perhaps well overdue, but again presumably depend very much on there being comparable organisations to the UK profession overseas.

- 3.6.5 Many general insurance actuaries work abroad from time to time, often for short periods. As a working party we were unsure whether general insurance had more or less actuaries working overseas relative to other areas of actuarial involvement. Certainly, the international nature of some non-life business has naturally involved general insurance actuaries in overseas work. Do such actuaries feel they have access to sufficient information concerning requirements that might be placed on them, and if not, who should provide this information?
- 3.6.6 One final intriguing question which arises is how quickly a move towards a European Institute might develop as a consequence of the Directive, as has happened already with Patent Agents.

4. SUPERVISION AND FORUM SHOPPING

- 4.1 The search for the most favourable EC country for Head Office location, in the light of the emerging Directives and local conditions, has been called "forum shopping". Whilst it is possible to distinguish between the physical and legal aspects of a Head Office location, this note and Appendix 3 assume they are the same.
- 4.2 The thought processes behind "forum shopping" would be very real for a Japanese or American company, looking to establish itself in Europe. Existing EC companies may, in practice, find it more difficult to change location although making skilful use of the law and holding companies/company structure could be an entirely practical consideration.
- 4.3 Appendix 3 lists a variety of criteria which might affect the choice of Head Office location. The working party's personal view of the relative importance of each criteria is given (high, medium, low). Some comment is also given against each criteria, together with appropriate EC directive references.
- 4.4 It is assumed that Head Office functions include:-
- o financial accounts consolidation;
 - o financial control;
 - o strategic control;
 - o public relations/image;
 - o shareholder relations - Board functions; and
 - o provision of central technical expertise including internal audits.

Functions such as Information Technology, "front line" underwriting, underwriting control, claims handling and control, policy issue/processing, sales, manpower/training are assumed to be non-Head Office functions. They could be carried out in the country of Head Office registration (home country), the country in which the business is written (host country) or a third country.

- 4.5 The reaction of existing shareholders and the taxation authorities to potential change is important. It may become theoretically possible for an existing quoted UK company to establish itself outside the UK. The reaction of the UK Inland Revenue to a larger tranche of UK business being removed from the UK tax net would be interesting!

- 4.6 Any decision to change would also depend upon company culture. The desired level of decentralisation, the corporate values and the future strategy would be crucial.
- 4.7 A review of this subject suggests that elements of the insurance process, such as product design, product coverage, competition, pricing, claims handling and so on are dependent on the host country and that Head Office location would not be important when the Services Directive is in force.
- 4.8 The key criteria affecting choice of Head Office location include: people issues, certain financial items, some communication and infrastructure issues and the degree and type of supervision. It is particularly interesting to note the importance of taxation and the degree of admissibility of the different technical reserves.
- 4.9 Change is taking place all the time, and even before the Framework Directive is enacted some of the current views may be out of date. Any decision on Head Office location would depend on the view taken of the speed of harmonisation and integration throughout Europe. Decisions taken on the basis of varying standards of supervision and disparate fiscal regimes could be negated as supervisory and tax harmonisation gains momentum. Furthermore, the cost of regular change to either physical or legal Head Office location could be significant.
- 4.10 In summary, it is felt that, in practice, there may be some adjustments made in the initial post services period but it is unlikely that Head Office locations will be changed on a regular basis in the longer run.

5. DISTRIBUTION

5.1 Introduction

- 5.1.1 This section summarises the current distribution pattern for personal lines business within the EC states, reflecting current and proposed legislation. Conclusions are drawn on the possible future evolution of the distribution of general insurance products.
- 5.1.2 There is, currently, relatively little data available on the distribution of non-life business within the EC compared to that available for life business. This is consistent with the amount of activity on distribution but is remarkable given the relative sizes of the two markets. As a result, much of the available data is a few years out of date. However, the distribution patterns are understood to be slow to change and so the picture painted by the available data is still believed to be relevant.
- 5.1.3 It is understood that detailed statistics on distribution are being collected by the ABI from the start of 1991 and should be available during 1992.

5.2 Current Position

- 5.2.1 Distribution patterns vary to a large extent in EC states! Details for each state are included in Appendix 1 attached. The following general statements apply:-
 - o most business is distributed through brokers and tied agents;
 - o direct marketing methods are relatively recent developments but they are growing rapidly in importance for some product lines;
 - o the trends of banks/savings banks/building societies becoming involved in distributing products and then moving on to take the profits of manufacture, a pattern which is well established for life business, are beginning to appear also for personal lines non-life business; and
 - o insurers are responding to these trends by searching for and developing new distribution methods, e.g. telesales.

5.3 Insurance Intermediaries Directive

- 5.3.1 Council Directive 77/92/EEC of 13 December 1976 concerns measures to facilitate the effective exercise of freedom of establishment and freedom to provide services in respect of the activities of insurance agents and brokers. The Directive was implemented in June 1978.
- 5.3.2 The purpose of the Directive is to provide for the freedom of establishment of insurance intermediaries and the freedom to provide services.
- 5.3.3 Some member states regulate the activities of insurance agents and brokers and make the taking up of these activities conditional on the possession of minimum levels of experience and training. The Directive specifies levels of training and experience for particular activities and member states must accept evidence that persons have met these levels in another member state as satisfying their own domestic requirements. In the UK, the DTI issues certificates of experience to people who can show they meet the requirements of the Directive, and these can be used to demonstrate the fact to the relevant authorities in other member states.
- 5.3.4 The categories of intermediary covered by the Directive are insurance brokers, agents and sub-agents.
- 5.3.5 In the case where no formal qualifications are required, as in the UK for instance, the Directive provides guidelines as to what is acceptable experience for operating in that capacity. In the UK, this is essentially provided by the DTI's certificate.

5.4 Other Directives

- 5.4.1 The Third Non-Life Directive includes the concept of insurers writing business across the EC on the basis of a single passport, supported by home state supervision. Host state controls are limited to those covering "general good" provisions, which may include distribution regulations - there may be varying interpretations of what constitutes a "general good" issue.
- 5.4.2 There appears to be no other current EC legislation affecting distribution.

5.5 Conclusions

- 5.5.1 Individual distribution patterns within EC states are likely to remain varied for the following reasons:-
- o the ability to maintain local regulation of distribution under host country "general good" provisions; and
 - o the different market structures regarding customers' product and distribution needs, will lead to different responses by intermediaries and insurance companies to commercial pressures.
- 5.5.2 The commercial pressures that will apply across the EC will lead to the following general evolution in personal lines:-
- o rationalisation of insurance markets leading to a reduction in the number of insurers;
 - o replacement of inefficient distribution systems;
 - o increasing involvement by banks and savings banks first in distribution then in manufacture for some non-life products (following their successes in life business);
 - o innovation in the development of new distribution methods for these products; and
 - o innovation in the development of products and services by other players that the banks and savings banks will have difficulty selling.

When asked to comment on the future of the insurance industry, Helmut Gies, Chairman of Aachen und Munchener, simply said "Distribution networks are what matters".

6. THE EFFECT OF EUROPEAN COMMUNITY COMPETITION LAW ON INSURANCE

6.1 The Treaty of Rome

Article 85 (1) of the Treaty of Rome finds that all agreements between undertakings, decisions by associations of undertakings and concerted practices which prevent, restrict or distort competition within the European community are prohibited as incompatible with the Common Market. However, any agreement which produces economic benefits outweighing anti-competitive effects may, under Article 85 (3) be exempted from Article 85 (1) on application. Moreover, the Commission has a general power to issue block exemptions under Article 85 (1) for specified classes of agreements.

6.2 Application to Insurance

- 6.2.1 Over the recent past the European Commission has held that Article 85 (1) extends to agreements between insurers. On several occasions, the practice of certain insurance markets within the Community was found by the Court to be contrary to the requirements of Article 85 (1). These decisions drew a distinction between unlawful rate fixing and beneficial collaboration in drafting policies or in gathering statistics.
- 6.2.2 As a direct result of the European Court of Justices' judgement in the German Fire Insurance case, the Commission's Competition Department received over three hundred notifications of agreements and recommendations from insurance companies which fell within the requirements of Article 85 (1). To a large extent these consisted of standard contracts or standardised terms of business used regularly and in large numbers by insurance companies when concluding contracts with policyholders, or as a basis for co-operation between insurance companies. The sheer volume of notification posed severe practical problems to the limited resources of the competition department and the Commission sought a general solution in the form of a block exemption.
- 6.2.3 To clarify matters, the Commission produced proposals for a Council of Ministers regulation authorising the making, by the Commission, of a block exemption relating to co-operation agreements between insurers. Following comments by the Economic and Social Committee and the European Parliament, the proposal was amended and the Council of Ministers, in June

1991, issued a regulation authorising the making of a block exemption within stated guidelines, the precise detail being left to the decision of the Commission.

6.3 The Council Regulation

- 6.3.1 Now that the Council of Ministers has adopted the necessary enabling regulations for the exemption, the detailed conditions of exemption can be established in Commission regulations expected to be in place by the end of 1992.
- 6.3.2 The regulation empowers the Commission, after consultation with insurance companies, associations and the Advisory Committee on Restrictive Practices and Monopolies to produce and adopt a block exemption regulation which will exempt any insurance agreements falling fully within its scope from being caught by the prohibitions contained in Article 85 (1) of the Treaty of Rome. Thus certain agreements involving insurance companies will be compatible with competition provisions of the Community, where the agreements have as their object co-operation with respect to:-
- o the establishment of common risk premium tariffs based on information or statistics collected by the participating parties;
 - o the establishment of common standard policy conditions;
 - o the common coverage or spreading amongst the companies of certain types of risks;
 - o the settlement of claims;
 - o the testing and acceptance of security devices; and
 - o registers of, and information on aggravated risks, subject to a guarantee of confidentiality.

6.4 Effects

The Council has adopted this enabling regulation as it seeks the benefits from the proper functioning of the insurance sector and the promotion of consumer interest which can emerge from co-operation between insurance undertakings. However, the Commission must, in formulating the provisions of the exemption, take account of the risk of competition being eliminated in a

substantial part of the market. Account must also be taken of any benefit which might be conferred on policyholders resulting from the agreements, and also of the risk to policyholders if the insurance sector becomes peppered with restrictive clauses. Sir Leon Britton believes that the block exemption will provide insurance companies with the legal clarity that they need to plan their community-wide activities.

7. EC THIRD NON-LIFE INSURANCE FRAMEWORK DIRECTIVE

Considerable detail on this evolving Directive was included in the report by the Working Party to GISG last year. This update summarises the current state of play and, after an outline of the contents of the draft Directive, examines the issues of interest arising in the continuing negotiations.

7.1 Background

- 7.1.1 The Directive will complete the framework for the conduct of non-life insurance inside the EC, using as a basis the principle of mutual recognition. Significant differences between member markets will, however, remain for some time, particularly in legal and fiscal areas.
- 7.1.2 The proposed Directive was published by the Commission on 31 August 1990. Since then interested parties in the UK and elsewhere have responded directly and indirectly, as has the European Parliament. Negotiations between the 12 countries are continuing in the hope that a common position can be reached by the end of this year. The UK is represented in Brussels by the DTI/GAD who are continuing the consultation process in the UK as appropriate.

7.2 Summary of the Requirements of the Directive

The detailed text of the draft Directive will be found in Appendix 4. Although there is general agreement that the Directive is to have a liberal approach, it should be noted that the final version could still look very different to the current draft.

7.2.1 Authorisation

A single authorisation to transact insurance is needed from the state in which a company's head office is located (the home Member State). This will allow branches to be set up, or insurance to be sold directly, in any other member state without the need for further authorisations in other states.

Requirements for authorisation are set out.

7.2.2 Supervision

Initial and continuing supervision will now be the responsibility of the home Member State.

Standards are outlined to achieve a degree of harmonisation with respect to technical provisions (as set out in the Accounts Directive) and the investment principles (spread, admissibility, currency matching, localisation and valuation of the assets covering the liabilities).

The types of assets which are allowed to cover the solvency margin are outlined.

No state may require the prior approval of premium scales and policy conditions.

7.2.3 Other Provisions

Considerable freedom is given to policyholders in choosing which member state's law shall be applicable to the contract of insurance.

Rules are outlined on the practical working of the freedom of establishment and provision of services concepts.

7.3 **Issues Arising**

- 7.3.1 Should subsidiary operations continue to be subject to supervision in their Home State rather than their parent's Home State? The European Parliament (EP) was keen that subsidiaries should be brought within the scope of the Directive and so subject to the supervision of the parent's Home State.
- 7.3.2 Is it necessary or feasible to harmonise contract law? Does this Directive and the Accounts Directive provide a sufficient basis for mutual recognition of supervisory systems?
- 7.3.3 The interaction with the Accounts Directive is important, for example, as regards the definition of technical provisions and the principles of calculation to be used.
- 7.3.4 Interaction with and/or implications for other areas and bodies, for example, IR, FSA, PPA, DTI, IOB, MIB, etc.

- 7.3.5 The EP seems to support a degree of systematic communication of policy conditions and rates to the member state of the risk though not prior approval under any circumstances. However, Article 26 looks like remaining as drafted.

Worries remain as to the use some supervisors may make of non-systematic notification.

- 7.3.6 Is Article 27 (systematic advance notification for compulsory insurance) a barrier to competition?
- 7.3.7 A clear definition of the concept of "general good", which limits host state control, is needed to clarify Article 25.
- 7.3.8 Some contributors want an early deadline for the termination of monopolies (Article 3) and some want to delete this article altogether.
- 7.3.9 Definition of 'qualifying holding'. Simplify to single 15% limit? See Articles 1 and 14. Ability to apply to courts in the event of opposition by a supervisory authority to shareholding changes?
- 7.3.10 Should localisation rule be more strict? (Article 15). The ability to hold assets outside the Community is important (sometimes compulsory), but should it be limited in some way?
- 7.3.11 Wording of Article 17 (investment principle for assets covering technical provisions). Should it cover all assets?
- 7.3.12 Additions/changes to list of admissible assets (Article 18). There is considerable debate about all the items of Article 18.1. It is a maximum list with member states able to have a narrower list. Issues raised include:

- broaden bodies covered by a) and b), for example, bonds, obligations or other money market instruments issued by an international organisation;
- loans granted to undertakings which are part of the same group;
- contractual loans offered to natural persons;
- commercial paper and unsecured loans;
- meaning of "variable yield participations";
- leased assets;
- broaden wording of i) (cash and deposits);

- clarify reinsurance items;
- clarify position of building society investments, preference shares;
- interests in limited partnerships;
- bank guarantees/letters of credit in support of reinsured amounts of technical provisions; and
- unquoted shares, warrants.

7.3.13 Additions/changes to the degree of admissibility list (Article 19). Like Article 18, this has generated considerable interest, with debate on the specific percentages, wording and scope. It is again a maximum list of items, applying to technical provisions with any additional assets being regarded as free assets. Specific issues include:

- should government stocks have a limit?
- percentages and wording of 19.1(c), for example, lower ceiling for hedging instruments?
- apply to gross or net technical reserves
- extend to limit the maximum equity investment in any one company?
- extend to consider the nature of the assets of a company whose shares are held as part of the technical reserves?

7.3.14 Investment policy implications, for example, of Articles 18 and 19.

7.3.15 Articles 18.2 and 19.3 are intended to be interpreted narrowly, allowing temporary deviations to the lists not permanent additions, for example, to cover an asset temporarily held by a company as a result of a borrower defaulting on a secured loan.

7.3.16 The investment of assets requirements of the Directive relate to the technical reserves only and not to free assets while the current UK provisions apply to insurers' investments as a whole. Should there be an investment principle on the assets supporting the minimum solvency margin? How will the assets representing the technical provisions be identified? Many commentators feel the matching of assets and liabilities principle is more important than arbitrary percentages - these need to be broad and flexible.

7.3.17 The ability of national authorities to allow stricter rules (for example, for Articles 18 and 19).

7.3.18 The UK "look-through" valuation of dependents and the grouping concession are not carried into the Directive. Should they be? Should there at least be a reference to taking account of the dependant's assets in order to assess an insurer's total exposure in any particular asset?

7.3.19 In the absence of more or less complete harmonisation in a given field, the national rules continue to apply. Such rules may lead to inequalities. UK insurers would want relaxation in UK requirements as necessary to allow UK insurers to compete on equal terms with those authorised in other EC member states.

For example the Directive does not contain valuation provisions - the UK could therefore continue to apply its existing valuation regulations, including the admissibility limits, alongside Articles 18 and 19, subject to there being no conflict. The ABI has drawn up a comparison of the current rules with those in the Directive.

The UK could thus be placed at a disadvantage from inter alia:

- UK current valuation/admissibility regulations including the dependent "look-through" basis;
- tax treatment of equalisation reserves, though this is not a direct concern of the Directive; and
- reinsurance conditions.

7.3.20 Strangeness of allowing 100% mismatching in ECU's (Article 21). Is this anticipating currency conversion?

7.3.21 Solvency margin items (Article 22). Debate has centred on the inclusion of subordinated loans:

- allow subordinated loans up to a 50% solvency margin (i.e. increase from 25%) in line with the Own Funds Directive;
- clarify the position of term and perpetual debt;
- the 25% is confirmed as applying to the required solvency margin, not the actual margin: any investments above the required margin could be by subordinated loan stock;
- is the 5-year run-off too short? Fully write down 1 year before redemption?
- term of any debt should be appropriate for the liabilities for which solvency cover is thus provided.

- 7.3.22 Clarify role and power of insurance committee (Article 42) in its ability to amend the Directive. Actuarial involvement needed, for example, re solvency/matching?
- 7.3.23 Should the host state get more powers before an undertaking can commence activities (Article 31)?
- 7.3.24 Include small mutuals and export credit insurance?
- 7.3.25 Separate accounts for health insurance?
- 7.3.26 Restrict grounds for refusing authorisation (Article 7)?
- 7.3.27 Should state be obliged to allow hidden reserves to cover technical reserves (Article 20) instead of having the option not to allow them?
- 7.3.28 Explain relation between "mandatory provisions" and "community law". See Article 24.
- 7.3.29 Freedom of establishment and freedom to provide services etc. provisions (Article 28 onwards) seem to be generating less disagreement and debate.
- 7.3.30 Local premium taxes. Article 41 rests uneasy within the free market concept.
- 7.3.31 Will all member states interpret Article 6.1 in the same way (for example, DTI "fit and proper persons" test)?
- 7.3.32 Importance of confidentiality of host country supervisors (Article 27) to avoid losing a marketing advantage.
- 7.3.33 Applicable law (Article 24) is presenting no serious problems in agreeing.
- 7.3.34 Impact on non-EC insurers.
- 7.3.35 Public availability of detailed information not addressed - wide variety throughout Europe.
- 7.3.36 The First Insurance Directive solvency requirements are maintained. Ultimately these may need to be re-considered. Periodic solvency report?
- 7.3.37 No provision on adequate/appropriate reinsurance or reinsurance with non-supervised reinsurers. UK supervision may be more onerous in this area.

- 7.3.38 Implication on actuarial guidance/knowledge adequacy of cross-border activity.
- 7.3.39 The position of composite companies is not mentioned.
- 7.3.40 The pooling of data may become more difficult.
- 7.3.41 What will the effect on policyholder protection be?
Following failure of an authorised insurer, perhaps the taxpayers in the home Member State will indemnify policyholders across the Community!

8. INSURANCE ACCOUNTS DIRECTIVE - NON-LIFE ASPECTS

8.1 Introduction

It has been recognised for a long time that some standardisation of the disparate fashion in which insurance operations prepare accounts across the Community was desirable. The necessary Directive to harmonise the control and presentation of accounts has been discussed in draft for years but, in June 1991, a common position was reached in the Internal Market Council. The European Parliament is now to give its view and, of course, further changes may ensue.

8.2 Summary of the Draft Directive

8.2.1 Date of the Directive

- o the deadline for the Directive to come into force is January 1, 1994. Member states are required to have the necessary legislation in place before that date;
- o insurance organisations are required to produce annual accounts and consolidated accounts complying with the Directive for financial years beginning on or after January 1, 1995 or calendar year 1995.

8.2.2 Provision for Review

The Council shall examine, and if need be revise, the provisions of this Directive in light of the experience gained in its first five years of operation. The ultimate aim is to achieve greater transparency and harmonisation.

8.2.3 Scope

The Directive applies to all "Insurance Undertakings". These are defined as:-

- o companies whose principal business is insurance;
- o groups which consist of one or more insurance organisations;
- o reinsurers; and
- o Lloyd's - covered by a separate annex.

8.2.4 Health Insurance

Where undertakings underwrite only health insurance wholly or principally according to the principles of life insurance, then the life insurance rules apply.

8.2.5 Deferred Acquisition Costs

Where acquisition costs are deducted from unearned premiums - the amounts deducted from the UPR must be indicated in the notes to the accounts. The basis must be compatible with that used for unearned premiums.

8.2.6 Unexpired Risks Reserves

The unexpired risk reserve should be shown under the heading Other Technical Provisions. They can also be included within the UPR subject to national legislation. If the provision is significant, it shall be disclosed separately either in the balance sheet or in the notes to the accounts. This suggests that the member states have the option to decide whether the UPR provision established by their companies is an unexpired premium plus unexpired risk reserve or if it is purely an unexpired premium reserve.

8.2.7 Outstanding Claims Provisions

These are defined as the estimated ultimate cost of settling claims, whether reported or not, less amounts paid.

8.2.8 Provisions for Bonuses and Rebates

The Directive suggests, in Article 29, that companies should make provisions for bonuses or premium rebates to the extent that these are due to policyholders or contract beneficiaries. This is consistent with the premium definition which includes estimates of ultimate premium levels. It also appears to be an effort to make a cleaner UPR, excluding such provisions.

8.2.9 Allocated Investment Return

The Directive allows member states to lay down procedures for the transfer of investment returns from one part of the P & L account to another. (In particular the UK can allow transfers of unrealised gains into the P & L). The reasons for the transfers, and the bases on which they are made, must be disclosed in the notes to the accounts. However, the use of averaging methods for capital gain which allow a gain greater than that of the year concerned to be brought into account will not be allowed.

8.2.10 Valuation of Assets

8.2.10.1 Assets can be valued at their current (market) values. The purchase price shall be disclosed in the notes to the accounts.

8.2.10.2 Where the valuation basis is purchase price, current values must be shown in the notes to the accounts.

8.2.10.3 In member states where investments are shown only at purchase price, they can defer disclosing the current value of investments for five years after the Directive comes into force, i.e. January 1, 2000. This is particularly relevant to the situation in Germany where the industry and the regulators are yet to be convinced of the merit of displaying current values in the accounts because of the potential local tax implications.

8.2.10.4 The valuation method must be shown in the notes to the accounts.

8.2.11 Technical Provisions

The total of all technical provisions should be sufficient to meet any liabilities arising out of insurance contracts as far as can be reasonably foreseen.

8.2.12 Unearned Premiums

- 8.2.12.1 Statistical methods of evaluation are allowed where they may be expected to approximate individual calculations.
- 8.2.12.2 Where risk does not arise evenly over the contract period the calculation method must take account of the different patterns in the emergence of the risk.

8.2.13 Outstanding Claims

- 8.2.13.1 Statistical methods may be applied to determine the level of provisions for outstanding claims. Member States, however, have the option to require prior approval of the methods before allowing companies to use the methods in their accounts.
- 8.2.13.2 Claims provisions shall include claims settlement costs irrespective of their origin.
- 8.2.13.3 Recoveries shall be estimated on a prudent basis. Where recoveries are material they must be disclosed in the notes to the accounts.
- 8.2.13.4 Structured settlements or claim benefits paid as an annuity must be calculated by recognised actuarial methods.
- 8.2.13.5 Implicit discounting is prohibited.
- 8.2.13.6 Explicit discounting is permitted subject to the following rules.
 - 1. The expected average settlement date of claims is at least four years after the accounting date.
 - 2. Discounting is effected on a recognised prudential basis.
 - 3. The supervisory authority must be given advanced notification of changes in method.

4. All factors which can cause an increase in costs must be included in the total cost of settling claims.
5. The company must have adequate data to construct a reliable model of the pattern and rate of claims settlements.
6. The rate of interest used in the calculation must not exceed a prudent estimate of the income available from the assets invested as a provision for claims over the settlement period.
 - The investment income cannot exceed income from such assets over the preceding five years.
 - The investment income also cannot exceed the income from such assets during the year preceding the balance sheet date.
7. The notes to the accounts should disclose the total amount of the provisions prior to discounting; the categories of claims which are discounted; the method and rates used; and the criteria adopted for estimating the period that will elapse before claims are settled.

8.2.14 Three Year Accounting

This is allowed under Article 61 method 1. This states that full claims reserves must be established not later than the end of the third year following the underwriting year.

8.2.15 Notes to the Accounts

The notes to the accounts must disclose gross written and earned premiums, gross claim charges, gross operating expense, and the reinsurance balance. They also need to split those figures into the main non-life classes where gross premiums in the class exceed ECU 10 million.

8.2.16 Consolidated Accounts

Consolidated accounts must be produced and the basis of consolidation must be specified.

8.2.17 Lloyd's

8.2.17.1 Lloyd's has been identified as a special case and is covered by the Annex to the main Directive. Both The Corporation of Lloyd's and Lloyd's syndicates are covered. The syndicates prepare annual accounts and the Corporation aggregate accounts. The aggregate accounts of the Corporation are meant to perform the same function as the consolidated accounts of other insurance undertakings.

8.2.17.2 The accounting basis for syndicates is Three Year Accounting.

8.2.17.3 Aggregate accounts must have a note giving details of inter-syndicate business, the treatment of run-off years of account, and the method of calculation of the premium income limit for the names.

8.2.17.4 There are rules for the disclosure of members' personal resources and Lloyd's central resources instead of Capital and free reserves.

8.2.17.5 Section B5(c) calls upon Lloyd's and Lloyd's syndicates to allocate income which derives from insurance contracts to syndicate years on an inception date basis not more than three years after January 1, 1994, the implementation date of this Directive. The previous draft gave Lloyd's five years to comply. This is a change from current practice and is likely to cause some difficulty.

8.2.17.6 Section B7 calls for all open years to be accounted for on a cash basis, yet section B5(d) states that reinsurance

recoveries shall be taken into account in open years where the syndicate has paid a claim. These requirements are clearly in conflict.

8.2.17.7 Operating expenses have to be allocated to the underwriting year of account for which they are incurred.

8.2.17.8 The disclosure required on closure of Lloyd's syndicates' three year accounts and the calculation of the "reinsurance to close" amount is specified.

8.2.17.9 Run off years of account are defined in section B9. The Directive states uncertainty prevents the determination of reinsurance to close. It does not specify actuarial involvement in the establishment of uncertainty for these purposes.

8.2.17.10 Lloyd's and Lloyd's syndicates are exempted from the requirement to disclose figures for deposits with ceding undertakings for three years after the Directive comes in force. After that period such disclosure will be required.

8.2.17.11 Life business written at Lloyd's will be treated in the same manner and subject to the same rules as non-life business.

8.2.18 Publication

Accounts must be published and made available to the members of the public. Any fee charged to the public for this service must be limited to administration costs.

8.2.19 Definition of an Actuary

The Directive refers to actuary and actuarial. It does not, however, define either of these terms. This implies that the member states may have to produce their own definitions of these terms when the implementation legislation is being produced.

8.3 Some Additional Issues Arising for General Insurance Actuaries

- 8.3.1 The accounts of the insurance company will need to show a 'true and fair' view. How strongly this underlying theme will be carried through from the company Accounts Directive and how much it will be tempered by the new Article 56,
- 'The amount of technical provisions must at all times be such that an undertaking can meet any liabilities arising out of insurance contracts as far as can be reasonably foreseen'
- remains to be determined. Considerable debate between actuaries and accountants as to the meaning of 'best estimates' is probable in this context.
- 8.3.2 The likely effect, as with the discussions on accruals profit reporting for life business, is for a very detailed annual audit examination of assumptions and methods of reserving to become the norm, if it is not already.
- 8.3.3 The changes to restrict discounting may lead companies to re-organise the claims classes they wish to discount in order to meet the new qualifying conditions. Some loss of historic data patterns may result; this may conflict with the need for 'reliable' historic data.
- 8.3.4 The Directive will force some significant changes for Lloyd's accounting - some aspects are still not clear.
- 8.3.5 There is still no European definition of an actuary.
- 8.3.6 The Directive is likely to cause more changes to UK disclosure (no hidden reserves in future) than on the continent, with the exception of disclosure of market values, still being fought by Germany to the bitter end.
- 8.3.7 No mention is made of distortions to the reporting of the performance of the Company which may arise from financial reinsurance or off-balance sheet financing.
- 8.3.8 Quite rightly, the rate of interest to be used for discounting is prospective but the limit on the rate to the past yield on the assets could be unsatisfactory. Sudden increases in inflation would increase the expected settlement value of claims and could cause depreciation in asset values.

APPENDIX 1: DISTRIBUTION PATTERNS IN EC STATES

The following pages contain information on distribution patterns available in published research.

1. Belgium
2. Denmark
3. France
4. Germany
5. Greece
6. Ireland
7. Italy
8. Luxembourg
9. Netherlands
10. Portugal
11. Spain
12. United Kingdom

1. BELGIUM

1.1 Distribution Channels

Most business is written through brokers and through agents who often represent one company only. Very little business is written direct with insurers.

Brokers are required to satisfy certain relevant education and experience criteria. Agents on the other hand are not subject to any control from the government or trade associations.

In general, Belgian non-life business must be placed in Belgium, though exceptions are given for certain large fire and liability risks, along with marine and aviation.

1.2 Top Ten Insurance Companies in 1986

Non-Life

<u>Rank</u>	<u>Company</u>	<u>Premium</u> B Fr billion	<u>Market Share</u> %
1	AG de 1830	15.01	10.1%
2	Royale Belge	13.70	9.3%
3	Cigna*	13.63	9.2%
4	ABB	9.82	6.6%
5	Cie Financiere Du Group AG	7.16	4.8%
6	SMAP Droit Commun	6.78	4.6%
7	Prevoyance Sociale	4.76	3.2%
8	Groupe Josi 1909	4.55	3.1%
9	Assurances Du Credit	4.51	3.0%
10	Drouot Assurances*	3.77	2.5%
TOP TEN TOTAL		83.67	56.4%
INDUSTRY TOTAL		147.76	100.0%

2. DENMARK

2.1 Distribution Channels

Until recently almost all business was conducted either direct with the insurer or through the companies' tied agents. Brokers are now permitted by law and are becoming established particularly in the area of large industrial risks.

2.2 Top Ten Insurance Companies in 1987

Non-Life

<u>Rank</u>	<u>Company</u>	<u>Premium</u> D Kr million	<u>Market Share</u> %
1	Baltica	3,537	16.0%
2	Topsikring	2,217	10.1%
3	Hafnia-Haand I Haand	2,070	9.4%
4	Tryg	1,390	6.3%
5	Alm Brand of 1792	1,351	6.1%
6	Kjobenhavnske Re	969	4.4%
7	Kgl Brand	954	4.3%
8	Hafnia	862	3.9%
9	Codan	851	3.9%
10	B-N Re (part of Baltica Group)	617	3.9%
TOP TEN TOTAL		14,818	67.2%
INDUSTRY TOTAL		22,036	100.0%

Note: These premiums represent the worldwide income of the companies mentioned. The top ten non-life companies hold approximately 50% of the Danish domestic market.

3. FRANCE

3.1 Distribution Channels

All intermediaries are subject to licensing regulations, which include maximum rates of commission which may be paid.

Recently, the market share held by mutuals, who do not use intermediaries, has been rising quickly. The mutuals have targeted particular occupational groups, such as doctors or farmers, and provide a complete range of policies for such groups. The mutuals now write 60% of personal motor business, and it is expected that they will become a greater force in other non-life personal classes.

In 1984 the Carrefour hypermarket chain began selling motor business and Habitat started selling householders' policies. It must be said that neither has apparently met with great success, nor many imitators. La Redoute, France's major mail order company, has launched the sale of general and life products (underwritten by one of the top ten companies).

Insurers in France have come under pressure from banks in non-life insurance, particularly for motor, household and medical insurance.

The banks have also begun to focus on opportunities in the property/casualty (non-life) insurance market. In France, as in many other European countries, this segment represents the lion's share of total insurance premiums. The banks believe that, in selected areas such as auto, household and medical insurance, their client relationships and their association with the lending business give them a competitive marketing advantage. Credit Agricole, for example, is setting up a new company to create and sell casualty insurance products, and several other banks have developed smaller non-life operations. The stock casualty insurance companies are also under attack from large mutual companies such as MACIF, MAAF and GMF. These institutions, working through salaried staff, have used low-cost structures to dominate the auto insurance market, and they now are increasingly turning their sales power toward the life, health and household insurance markets.

Respondents to a recent survey highlighted the following as key emerging distribution channels:

- direct response advertising,
- direct mail,
- affinity groups,
- merchandising retailers,
- home network (videotext).

Cont/d

3.2 Top Ten Insurance Companies in 1987Non-Life

<u>Rank</u>	<u>Company</u>	<u>Premium</u> F Fr billion	<u>Market Share</u> %
1	AXA-Midi	16.49	9.6%
2	AMA	15.77	9.2%
3	UAP*	15.39	8.9%
4	AGF*	10.54	6.1%
5	GAN*	7.70	4.5%
6	Mutuelle Du Mans	7.57	4.4%
7	MACIF	6.77	3.9%
8	GMF	5.51	3.2%
9	MAAF	5.08	3.0%
10	Victoire	4.67	2.7%
TOP TEN TOTAL		95.49	55.5%
INDUSTRY TOTAL		172.00	100.0%

Note: These tables show group, rather than specific company, income.
This demonstrates more appropriately the power blocks in the market.

4. GERMANY

4.1 Distribution Channels

Unusually, in a strongly-regulated environment, there is no regulation of brokers other than the normal application of commercial law.

Around 75% of individual life and non-life insurance policies are arranged through direct sales forces in Germany at present.

Banks and savings banks will assume a significant role as distributors in future - although this is mainly for life business, there are examples emerging already in non-life business.

4.2 Top Ten Insurance Companies in 1987

Non-Life

<u>Rank</u>	<u>Company</u>	<u>Premium</u> DM billion	<u>Market Share</u> %
1	Allianz	6.19	11.0%
2	Colonia	2.10	3.7%
3	Gerling Allgemeine	2.04	3.6%
4	R + V Allgemeine	1.80	3.2%
5	HUK-Coburg	1.72	3.1%
6	HDI	1.45	2.6%
7	Frankfurter	1.40	2.5%
8	Gothaer Versicherungsbank	1.34	2.4%
9	Victoria	1.28	2.3%
10	Landwirtschaft Vers V Munster	1.27	2.3%
TOP TEN TOTAL		20.58	36.6%
INDUSTRY TOTAL		56.25	100.0%

Source: BAV Geschäftsbericht 1987

Note: All figures exclude health premiums, which in 1988 amounted to DM 14.9bn.

5. GREECE

5.1 Recent Developments

Between 1985 and 1987 the non-life market grew by 56% (life market by 80%).

5.2 Distribution Channels

The key feature is the domination of the market by state-controlled insurers, who in 1985 held over half the total life/non-life business.

Brokers, agents and sole company agents are all present and active. Direct placing of business between the insurer and insured is common. Commission levels are subject to control by the state.

The state-controlled banks tend to use their influence to direct customers' business to their large insurance subsidiaries, even though such pressure is not condoned by the law.

5.3 Top Ten Insurance Companies in 1987

Non-Life

<u>Rank</u>	<u>Company</u>	<u>Premium</u> Drs million	<u>Market Share</u> %
1	Ethniki*	9,664	21.2%
2	Agrotiki*	4,868	10.7%
3	Phoenix*	4,460	9.8%
4	Astir*	4,198	9.2%
5	Panellinios	1,714	3.8%
6	Intertrust	1,658	3.6%
7	Magdeburger	1,261	2.8%
8	AGF-Kosmos	1,063	2.3%
9	Europaiki Pistis	954	2.1%
10	Ioniki	934	2.1%
TOP TEN TOTAL		30,774	67.5%
INDUSTRY TOTAL		45,553	100.0%

6. IRELAND

6.1 Recent Developments

The Irish Government is keen to encourage the development of Dublin as an international financial services centre and offers a low rate tax for designated financial services, including insurance. It is hoped that the centre will attract life and non-life insurers, captives, and insurance broking and captive management companies. A number of projects have been announced and it is hoped that there will be further developments in this area in the next year.

6.2 Top Ten Insurance Companies in 1987

Non-Life

<u>Rank</u>	<u>Company</u>	<u>Premium</u> I £ million	<u>Market Share</u> %
1	Hibernian	109.7	15.8%
2	PMPA	81.5	11.8%
3	Guardian Royal Exchange*	69.6	10.0%
4	Insurance Corp'n	55.4	8.0%
5	Sun Alliance	50.8	7.3%
6	Shield*	40.5	5.8%
7	General Accident*	37.6	5.4%
8	Church and General	33.1	4.8%
9	Irish National*	32.5	4.7%
10	Royal*	30.7	4.4%
TOP TEN TOTAL		541.5	78.0%
INDUSTRY TOTAL		693.2	100.0%

7. ITALY

7.1 Distribution Channels

A number of the major international brokers are present, but Italy is not yet a broker-dominated market. Regionalism is a feature of Italian life, and this works in favour of the smaller broker and particularly the smaller agents, often tied to a single company, who dominate the distribution network for all but the largest commercial and industrial risks.

Regulations prevent brokers from placing more than a fixed proportion of the business with a single insurer.

Brokers and agents normally obtain professional qualifications from their associations; both brokers and agents are required to be licensed.

Direct writing is unusual.

Insurance and banking links are being forged, eg those between Generali and Banca Commerciale. However, banks are not generally active in the sale of savings products, whether insurance-based or otherwise.

The agents are gradually losing some of their market share to brokers. The erosion of the agents' position is aggravated by the Ministry of Industry's encouragement of other distribution channels such as mail order for the sale of "simple" products.

There has been an increase in the number of joint ventures between banks and brokers as brokers realise that the bank branch networks are a ready-made distribution channel for their products. The large brokers Nickols have set up subsidiaries with different banking partners in different areas - "Brosel" in the north west and "Brokerban" in the north east of the country, reflecting the regionalism that remains a feature of Italian life. Banks are seeing the attractions of selling insurance to the general public. Cariplo, for example, has launched a new broker called Paros.

7.2 Top Ten Insurance Companies in 1987

Non-Life

<u>Rank</u>	<u>Company</u>	<u>Premium</u> Lire billion	<u>Market Share</u> %
1	Generali	1,530.0	8.5%
2	SAI	1,289.0	7.1%
3	Assitalia	1,260.0	7.0%
4	RAS	1,173.0	6.5%
5	Lloyd Adriatico	676.0	3.7%
6	Unipol	665.5	3.7%
7	Toro	559.0	3.1%
8	Fondiarria	554.0	3.1%
9	Reale Mutua	495.5	2.7%
10	Italia	447.0	2.5%
TOP TEN TOTAL		8,649.0	47.8%
INDUSTRY TOTAL		18,084.0	100.0%

8. LUXEMBOURG

8.1 Distribution Channels

Tied agents are the commonest intermediaries and in 1986 numbered about 5,000.

Brokers, who are regulated, concentrate on industrial risks.

Direct writing is common for personal business.

8.2 Major Insurance Companies in 1986

Non-Life

<u>Rank</u>	<u>Company</u>	<u>Premium</u> L Fr million	<u>Market Share</u> %
1	Le Foyer	2,618	30.1%
2	La Luxembourgeoise	1,859	21.4%
3	Assurlux	373	4.3%
TOTAL		4,850	55.8%
INDUSTRY TOTAL		8,694	100.0%

9. NETHERLANDS

9.1 Distribution Channels

The market includes brokers, tied agents and independent agents. All intermediaries must be registered; the degree of expertise to be demonstrated (by examination) depends on the type of intermediary. There are over 30,000 intermediaries registered. A significant share (perhaps 25%) of business is written direct between insurers and their customers.

Approximately 45% of premiums are sold by intermediaries, mostly independent retail brokers and a small number of tied agents. About 2,000 are responsible for 80% of the total turnover through brokers. These intermediaries work for on average ten insurers. They must register with the Social Economic Board (SER) which currently has about 30,000 intermediaries enrolled.

Under the Assurance Mediation Act (WAB), intermediaries need to pass examinations before being registered. There are four categories of intermediary: A, B, C and D. Those in category A have passed the most difficult examinations and are considered the most professional. Those in category D have passed relatively easy examinations. The act is currently being amended to remove categories C and D, which account for approximately 27% of intermediaries, so as to increase their professionalism. As a result it is expected that the number of intermediaries will have decreased by 1 January 1991.

Large insurers sometimes also work with captive agents (an agent whose shares are owned by an insurance company), but because these are not registered in the Netherlands it is difficult to establish whether an insurance company has captive agents. Banks functioning as a broker are also an important channel of distribution with approximately 10% of total market turnover in 1989. About 20% of insurance is sold directly (through advertising or telephone sales) and 20% is sold via specialist commercial insurance brokers. Direct sales forces and merchandise retailers account for the majority of the remainder.

9.2 Top Ten Insurance Companies in 1987

Non-Life

<u>Rank</u>	<u>Company</u>	<u>Premium</u> D Fl billion	<u>Market Share</u> %
1	Nationale-Nederlanden	1,578	9.9%
2	Zilveren Kruis	1,013	6.3%
3	Aegon	893	5.6%
4	Delta Lloyd*	801	5.0%
5	Interpolis	630	3.9%
6	Nieuw Rotterdam	486	3.0%
7	Amev	483	3.0%
8	OHRA	443	2.8%
9	Royal Nederland*	374	2.3%
10	Central Beheer	373	2.3%
TOP TEN TOTAL		7,074	44.2%
INDUSTRY TOTAL		16,003	100.0%

Cont/d

9.3 Sales of Insurance to Individual Clients in the Netherlands, 1988

	<u>Life</u>	<u>Non-Life</u>	<u>Total</u>
	<u>£</u>	<u>£</u>	<u>£</u>
Brokers/Agents	68	39	45
Banks	10	9	10
Direct	15	32	28
Employer	1	17	13
Others	6	3	4
Total Sales	D Fl 2,750	D Fl 9,850	D Fl 12,600

10. PORTUGAL

10.1 Distribution Channels

Brokers and agents must be authorised by the Instituto de Seguros de Portugal, which also determines appropriate commission levels. Basic education standards are imposed on all intermediaries. Agents may be either independent or tied to one insurer. There are some 30 broking firms, 10,000 tied agents and 30,000 other agents (including part-time intermediaries).

In common with other European countries, banks and hypermarkets are both making their mark on the traditional distribution channels.

The majority of business is, however, placed direct with insurers without recourse to intermediaries.

10.2 Top Ten Insurance Companies in 1986

Non-Life

<u>Rank</u>	<u>Company</u>	<u>Premium</u> Esc million	<u>Market Share</u> %
1	Imperio	18,770	13.1%
2	Mundial Confianca	18,437	12.9%
3	Fidelidade-G Segurador	15,720	11.0%
4	Bonanca	14,665	10.3%
5	Tranquilidade	14,536	10.2%
6	Alianca Seguradora	12,327	8.6%
7	Portugal Previdente	4,916	3.4%
8	Trabalho	4,764	3.3%
9	Metropole	4,423	3.1%
10	Garantia	3,545	2.5%
TOP TEN TOTAL		112,103	78.5%
INDUSTRY TOTAL		142,800	100.0%

Source: Instituto de Seguros de Portugal

11. SPAIN

11.1 Distribution Channels

Regionalism plays a part in determining distribution networks. Many small companies (often mutuals) cater for local insurance needs. Whilst brokers are well-established for larger risks, tied and independent agents control the bulk of business in both the life and non-life sectors. Both agents and brokers are required to be licensed; the decree of 6 July 1988 tightened up the regulations as to who can sell insurance or act as a broker, including the unusual provision that insurers may own broking houses.

Direct writing is becoming increasingly popular, as a means of bypassing the established distribution channels and lowering acquisition costs.

The role of banks is important and contentious; many Spanish banks have extensive branch networks and they are seeking to exploit these to market insurance products. A number of banks have gone further, and purchased insurance companies whose products are then sold through the bank's branches. This penetration of the insurance market by banks is unusual in Europe and demonstrates the confidence of Spanish banks in the future potential of the insurance industry.

However, in the non-life sector - and perhaps in the life sector, as well - banks' cost advantage must be set off against the widely acknowledged barriers of marketing complex products and settling claims involving banking clients. Of the banks followed in detail, only BBV has yet entered the property and casualty sector. The industry clearly is proceeding with caution. Quite apart from the universal issue of whether bank staff - however motivated and trained - can sell volumes of life and pension products, bank distribution of non-life products raises a variety of other issues: For example, will bank employees be able to make effective risk judgments? Will problems arise in adjudicating claims when the claimant is a valued customer of the branch? What will determine the ultimate loss experience in the non-life business?

11.2 Top Ten Insurance Companies in 1987

Non-Life

<u>Rank</u>	<u>Company</u>	<u>Premium</u> Ptas million	<u>Market Share</u> %
1	Union y el Fenix Espanol (B)	39,384.6	5.4%
2	Mapfre Belge	36,452.8	5.0%
3	Mutua Madrilenia Automovilista	32,296.9	4.4%
4	Winterthur*	21,684.2	3.0%
5	Group Vitalicio	20,279.3	2.8%
6	Santa Lucia	19,842.7	2.7%
7	Sanitas	16,355.9	2.2%
8	Asistencia Sanitaria Interprov	16,019.8	2.2%
9	Ocaso	15,942.4	2.0%
10	Mutua Nacional Del Automovil	14,527.4	2.0%
TOP TEN TOTAL		232,786.0	31.9%
INDUSTRY TOTAL		729,736.0	100.0%

12. UNITED KINGDOM

12.1 Distribution Channels

The title "broker" may only be used by intermediaries registered with the Insurance Brokers' Registration Council. Other intermediaries in non-life insurance may trade under other titles without any form of regulation, though a Code of Practice has been applied by ABI members to their agents from 1 January 1989.

12.2 Top Ten Insurance Companies in 1988

Non-Life

<u>Rank</u>	<u>Company</u>	<u>Premium</u> £ million	<u>Market Share</u> %
1	Sun Alliance	1,429	11.3%
2	Royal	1,193	9.4%
3	Eagle Star	956	7.6%
4	General Accident	946	7.5%
5	Commercial Union	901	7.1%
6	Norwich Union	840	6.6%
7	Guardian Royal Exchange	690	5.5%
8	Prudential	428	3.4%
9	Co-operative	423	3.3%
10	Cornhill	404*	3.2%
TOP TEN TOTAL		8,210	64.8%
INDUSTRY TOTAL		12,652	100.0%

Note: These figures represent the UK non-life premium income of these companies, except for Cornhill, which is the worldwide income.

12.3 Specific Examples

Royal Bank of Scotland

The Royal Bank of Scotland has undertaken two recent insurance initiatives. It formed Direct Line - a new, high-technology auto insurance distribution subsidiary that is among the fastest-growing insurance companies in Europe - and it has just formed a joint venture life insurance company with Scottish Equitable, one of Scotland's leading insurers. In developing its insurance strategy, it is believed that RBS carefully considered the key issues of product line and distribution strategy and decided against offering general insurance products through its branches for the following important reasons:

- It lacked the management skill to understand the product risks fully. General insurance products are based on the assumptions that losses will occur (actuarial risk); bankers are more familiar with credit risk, which typically assumes a statistical loss ratio only at the margin, with loans initially underwritten in the belief that they will be repaid.

Cont/d

- Customers purchase most casualty and general insurance products because they require the insurance: marketing studies have shown that, in such cases, customers become more selective.
- Most casualty insurance policies are rolled over at the end of their term, typically one year, which gives the existing insurer a huge competitive advantage. The existing policy is often cheaper than a new one, because the customer initially shopped around for the cheapest quotation, and a no-claims history reinforces this downward pressure. A new player, therefore, would be likely to attract less desirable business.
- Where insurance is linked with a credit product - for example, in household insurance - RBS was in a weak position, particularly relative to the building societies, in view of its limited mortgage business.

As a result, RBS opted to enter only the life insurance and pensions business directly, regarding this segment as more appropriate to its customer base, easier to sell because of the savings dimension and much safer in terms of underwriting risks. Its general insurance strategy centres on Direct Line, which is clearly separate from the bank.

Direct Line - A Dedicated Retail Non-Life Channel

Royal Bank of Scotland's Direct Line subsidiary is a relatively new automobile insurance company that has achieved superb growth rates by being a low-cost and very efficient provider. Direct Line underwrites its own policies and keeps its costs very low by not using agents or intermediaries to distribute its product; instead, it sells directly to the customer. The subsidiary has researched the market carefully to identify particular risk categories with which it is comfortable.

TSB

General insurance - auto, household, travel, and sundry protection policies - are sold in bank branches by bank employees. These products require little expertise to sell, because they are based on standard premium rates and are usually attached to an underlying credit facility. TSB sells mutual funds through the life and pensions sales force and a variety of other distribution channels such as direct mail, independent agents and other financial institutions that do not have their own in-house product.

SINGLE MARKET INSURANCE LEGISLATION

Measure	Current Status	Implement. Date	Reference	Comments
The annual accounts of insurance companies	Proposal submitted to Council 21.1.87 * E.P. Opinion given Amended proposal 25.10.89		C131, 18.5.87 C96, 17.4.89 C30, 8.2.90	Projected date of adoption by Council 1991 Qualified Majority First Reading
The winding up of insurance companies	Proposal submitted to Council 23.1.87 E.P. Opinion given Amended proposal 18.9.89		C71, 19.3.87 C96, 17.4.89 C253, 6.10.89	
Insurance contracts	Proposal submitted to Council. E.P. Opinion given 10.7.79 Amended proposal 31.12.80 Proposal to be withdrawn or substantially amended; law relating to contracts features in Third Non-Life Directive		C190, 28.7.79 C265, 13.12.80 C355, 31.12.80	
"Non-Life" insurance: freedom to provide services (Second Non-Life)	Adopted 22.6.88 Directive 88/357/EEC	29.06.90 Derogations for Spain (1.1.97); Greece, Ireland & Portugal (1.10.98).	L172, 4.7.88	Amending Dir. 73/239/EEC
Legal expenses insurance	Adopted 22.6.87 Directive 88/344/EEC	1.7.90	L185, 4.7.87	
Credit and suretyship insurance	Adopted 22.6.87 Directive 87/343/EEC	1.7.90	L185, 4.7.87	
Life assurance: freedom to provide services (Second Life Directive)	Adopted 8.11.90 Directive 90/619/EEC	20.5.93 (derogations) Certain transitional provisions will apply for Spain until 31.12.95 and Greece and Portugal until 31.12.98 and for all Member States until 31.12.94	L330, 29.11.90	Amending Dir. 79/267/EEC
Motor vehicle liability insurance: freedom to supply services	Adopted 8.11.90 Directive 90/618/EEC	20.11.92	L330, 29.11.90	The Mass Risks aspect of the dir. (home country control) will only enter into force after adoption of the 3rd non-life directive; as a result, the mass risks regime foreseen in the 2nd non-life dir. (Dir.88/357) will not be entirely applicable until the 3rd non-life dir. has been implemented.

Motor vehicle liability insurance: Third Directive	Proposal submitted to Council 23.1.88 EP first opinion 25.10.89 Common position EP second opinion 14.3.90 Adopted 14.5.90	31.12.92 Derogations for Greece, Spain & Portugal until 31.12.95 for Articles 1&2; Der. for Irl. until 31.12.98 regarding pillion passengers of motorcycles under Art.1 until 31.12.95 to comply with Art.1 as regards other vehs & to comply with Art.2	C16, 20.1.89	
Insurance: application of competition law	Proposal submitted to Council 21.12.89 EP first opinion 10.09.90 Amended Proposal 12.1.91		C16, 23.1.90 C8, 12.1.91	
EC insurance committee to assist Commission in its work	Proposal submitted to Council 18.7.90 ESC opinion 13.02.91		C230, 15.9.90	
Non-Life Framework Directive (Third Non-Life Insurance Directive)	Proposal submitted to Council 18.7.90 * ESC opinion 11.02.91		COM (90)348 31.08.90	Projected date of adoption by Council 1991 * * Qualified Majority
Life Framework Directive (Third Life Assurance Directive)	Proposal submitted to Council 20.02.91 *		COM(91)57 to be published	Projected date of adoption by Council 1992 * * Qualified Majority
Pension Funds	Not yet submitted: proposal expected by August 1991 (Commission working paper)		(Nov. 1990)	
Guarantees given by banks and insurance companies	Proposal submitted to Council EP first opinion 14.02.90 ESC opinion Amended Proposal 25.1.91		CS1, 28.02.89 C93, 19.03.90 C159, 26.06.89 COM(90)567	
Consumer Protection: Contract Terms	Proposal submitted to Council 06.07.90		COM(90)322	
EC Reinsurance Pool for Central and Eastern Europe	Proposal submitted to Council		C302, 1.12.90	
Insurance Accounts Directive	Proposal submitted to Council 07.91	12.91 Introduced by 1.1.95 for Ins. Accounts		

* presented since the publication of the White Paper (14 June 1985)

* * await European Parliament Opinion or First Reading

Pre-Single Market Insurance Legislation

Adopted Directives - Insurance Supervision

<i>Measure</i>	<i>Date of Adoption</i>
Reinsurance: freedom of establishment and freedom to provide services	25.02.64
Non-Life Insurance: freedom of establishment (First Non-Life Directive)	24.07.73
Insurance Intermediaries	13.12.76
Co-Insurance	30.05.78
Life Assurance: freedom of establishment (First Life Assurance Directive)	05.03.79

Adopted Directives - Classes of Business

<i>Measure</i>	<i>Date of Adoption</i>
First Motor Insurance Directive	24.04.72
Second Motor Insurance Directive	30.12.83
Tourist Assistance	10.12.84

FORUM SHOPPING

<u>CRITERIA</u>	<u>IMPORTANCE OF CHOICE OF H.O. LOCATION</u>	<u>RELEVANT DIRECTIVE/COMMENT</u>
<u>PRODUCT:</u> Demand	L	Framework directive, coinsurance directive, services directive for large risks, compulsory motor directive, legal expenses and credit insurance directives. Demand depends on general economic conditions which are expected to improve as the EC develops.
Coverage/wordings	L	Framework directive - host country is the determining feature, particularly for mass risks.
Pricing - flexibility	L	Framework directive - depends on host country conditions.
Competition	L	Framework directive, freedom of capital movement directive, establishment directives, EC directorate DGIV and the block exception for some items - host country dependent in light of number of competitors/pricing policies.
<u>CLAIMS:</u> Legal background/courts	L	No specific directive on operation of courts - depends on host country legal system. On the whole, framework directive assumes most favourable treatment in host country.
Society/culture	L	Depends on host country attitudes to insurance claims.
on the spot service	L	Claims handling preferably carried out in host country to give quality of service.

CLAIMS: (Continued)
Service levels

M

Host country standards likely to determine required level of service; some form of control may be required which could be weakened if too far geographically separated from host country.

Client information

L

Host country dependent.

Claims costs and control

L

In the main dependent on host country control although subject to overriding policy decisions by Head Office (claims processing could be in a third country with or without the use of local agents). Impact of EC on inflation, exchange rates (EMU/ECU), pollution, salary awards, spare parts and so on can all be influenced by overall EC trends but mainly host country based.

Claims incidence (risk factors)

L

As for costs - host country based.

DISTRIBUTION:
Means/type

M

EC interest shown in standard of education/control of intermediaries but as yet no substantive directive: distance of Head Office can impact relations and therefore make choice of Head Office location an issue.

Local image

L

Host country dependent.

Costs

L

Competition directive affects ability to maintain standard rates of commission - becomes a host country dependent issue.

Bargaining power

M

Head Office location may effect the degree of "leverage".

Quality of distribution

M

As for bargaining power.

PEOPLE:

Skills - local	L	Host country dependent.
Skills - Head Office	H	Dependent on Head Office functions - see definition in body of report - an important issue in choosing Head Office location although moving skilled people into a country maybe a solution.
Demographics	M	Most countries "suffer" similar population age patterns - labour supply/demand might be a consideration.
Labour costs/remuneration and Union relationships	M	EC social directives on Board membership may be an issue and certainly varies at present with home country: wages vary between country and seem likely to harmonise in the foreseeable future.
Processing	L	Could be host country, home country or third country!
Technical/management skills	H	An important quality issue - depends on the functions of Head Office but some will be in the home country even if others are host country based.
Training/education	H	See comments above on technical/management skills; very much a quality issue which may vary with choice of home country.
Pensions (costs and availability)	H	EC directive on Pan European pensions schemes may impact: costs and requirements at present depend on choice of home country.
Mobility	M	The staff must be prepared to travel to and from host countries - no restrictions on mobility by EC law: choice of suitable Head Office location could entice skilled personnel to move there.

PEOPLE: (Continued)
Culture/ethos

H

Local ethos can be overridden but this is an important issue in the style of the Management team.

Languages

H

As yet no directive exists to harmonise languages
- multi-lingual staff may be of value!

FINANCIAL:
Investment availability/
access

L

Directive enables capital movements across boundaries - accounts directive requires matching of technical reserves therefore a host country issue.

Taxation - absolute level

H

No specific directive although harmonisation may occur in time as "market forces" take effect.

Taxation - scope/coverage

H

As for taxation above, note also that tax authorities may object to change of tax net: (particularly if a block of business is transacted in given country and Head Office relocated to different tax area).

Accounts format

M

Accounts directive as interpreted in home country - could be of some consideration.

Cash flow

L

No impact: capital movement directive permits complete exchange control/remitability freedom.

Shareholders'needs/
culture

L

No particular directives but if publicly quoted a very important issue: otherwise not particularly relevant.

Reserves - general adequacy

M

Links with points under supervision heading.

Reserves - discounting

M

Supervision and accounts directive refer - could be an issue if some home countries permit more flexibility than others.

<u>FINANCIAL:</u> (Continued)		
Solvency	L	See heading supervision.
<u>SYSTEMS/IT:</u>		
Technology available -- hardware	M	Complete availability in theory but in practice may not be easy to access.
Technology available - software	M	As for technology - hardware: data protection directive may impact.
Communications	H	No particular directives and, although in theory easy, in practice may be an issue in some countries.
Distributed processing	M	No particular directives: IT processing could be distributed to host country or third country. However, Head Office location could be an issue.
<u>SUPERVISION/CONTROL:</u>		
Authorisation levels and style/depth of supervision	H	Could be a significant issue - depends on the cost and complexity of the supervision. As yet no directive exists to fully harmonise and home states have freedom of choice of style.
Reliability of supervision	M	Unreliable supervision leading to insolvencies could affect the reputation of a home country insurance company. However, this is not a major issue given status of company: relationship with supervisors could be an issue if not of a harmonious nature.
Classes of business	L	Establishment and framework directives refer - now harmonised across all countries.
Responsibilities	H	An important issue for some aspects of the business: depends on how dominant the supervisory regime is and what the responsibilities of directors, auditors and so on are.

SUPERVISION/CONTROL: (Continued)

Directors	H	Directors need home country approval: they need to know the local law and practice: if they are not locals then there might be some problems in this respect: any Union rules/regulations regarding staff directors could be a consideration.
Auditors	M	Audit quality could be an issue in some countries: accounts directive refers but relationships with auditors can be important.
Actuaries	L	With the advent of the diplomas directive this is not really an issue and skills can be transferred from any European location to another.
Solvency/financial strength	H	Despite accounts directive, attitudes can vary between country and will affect the way a company is run and potentially rate of return on capital: the degree of harmonisation may improve as market forces tend to reduce discrepancies between countries.
Company law/Articles of Association	M	EC directive on company law makes this less of an issue than it perhaps could have been.
<u>GENERAL:</u> Political climate	H	No specific directives but rate of implementation of directives important - political stability could be a feature requiring careful consideration in choosing Head Office location.
Economic climate	M	Economic climate of host country far more important but nevertheless a consideration.

GENERAL: (Continued)

Market intelligence - third party views	M	Analysts reports on insurance activity and competitor activity could be an issue requiring consideration - particularly as far as shareholder views are concerned.
Market intelligence - competitor exchanges	M	Tends to be host country based and therefore of less relevance at Head Office level: nevertheless an issue worth considering.
Data availability	M	Insurance framework directive does not encourage availability of industry wide information therefore approach in home country could be an issue if it varies from approach in host country.
Data analysis - management info.	L	Host country dependent.
Access/travel	H	Air access particularly important - might influence some to look for central EC location to minimise total travel bill.

COMMISSION OF THE EUROPEAN COMMUNITIES

COM(90) 348 final - SYN 291

Brussels, 31 August 1990

Proposal for a
THIRD COUNCIL DIRECTIVE

on the coordination of laws, regulations and administrative
provisions relating to direct insurance other than life
assurance and amending Directives 73/239/EEC and 88/357/EEC

(presented by the Commission)

EUROPEAN COMMUNITIES
THE COUNCIL

Brussels, 18 July 1991

7367/91

RESTREINT

SURE	31
DRS	29
PRO-COOP	66

COMMON POSITION
ADOPTED BY THE COUNCIL ON
WITH A VIEW TO THE ADOPTION OF A DIRECTIVE
ON THE ANNUAL ACCOUNTS AND CONSOLIDATED ACCOUNTS
OF INSURANCE UNDERTAKINGS