European Competition Policy for the Insurance Market

Wulf-Henning Roth *

A. Introduction

The legal environment of the European Insurance Market has undergone a radical change in the last 10 years: National regulations on insurance supervision have been deregulated in order to open the national, traditionally intensively regulated insurance markets for community-wide competition. In a more or less parallel action, the Commission discovered its competence to enforce the EC competition rules in the insurance sector. In the early 1990's, the Commission issued a Block Exemption Regulation concerning co-operation within the insurance sector with respect to certain agreements. This development has come as a surprise for some analysts: The endeavour of the Commission to deregulate the national insurance markets had been conceived as being based on the general philosophy that state regulation of the insurance business, especially in the field of premiums and policy conditions, is undesirable from a competition perspective. This view has been put into question by the Block Exemption Regulation that gives the insurance industry substantial leeway to co-operate exactly in these fields. In the end, the impression may be that the regulation of insurance activities has been taken away from the responsibility of the state authorities and transferred to the industry itself. It is contended that the Commission's primary goal was rather to break down the national insurance markets in order to create a

* Dr. jur. (Munich), LL.M. (Harvard), Director of the Centre for European Economic Law, Professor of Law at the University of Bonn Law School.
This paper was presented at the Antitrust and Unfair Competition Conference at The College of Management — Academic Studies Law School, May 25-26, 1998, in Rishon Lezion (Israel). The later published Report of the Commission on the application of Reg. 3992/92 of May 12, 1999, Com (1999) 192 final and the position of the Economic and Social Committee, O.J. 2000 C 51/105, have been taken into account.

common insurance market, and only to a lesser degree to develop and pursue a coherent competition policy with regard to the insurance industry.

B. European competition policy

I. The background [1]

Though the competition rules of the EC Treaty do not provide an exemption for the insurance sector, the Commission did not become active in this area before the early 1980's[2]. One of the two Commission decisions — the *Fire Insurance* decision[3] — was appealed, leading to the judgement of *Verband der Sachversicherer v. Commission* of the Court of Justice of January 27, 1987[4]. This judgement may fairly be considered as the basis and trigger for a truly European competition policy in the insurance business.

This somewhat belated start of a European competition policy on insurance can be traced back to essentially two interrelated reasons: The existence of an intensive state regulatory system in some member states[5] and the so-called "special characteristics" of the insurance industry that have traditionally been regarded, at least in some member states, as justifying a special regime in the national competition laws.

II. Existence of state regulatory systems

The existence of an intensive regulatory system in some of the Member States had the consequence that except for re- and co-insurance, most insurance markets were basically national markets. Co-operation in the insurance sector

1 The sources of European Community competition law comprise different elements. The most important element is the EC Treaty which is the primary source of Community law. Treaty Establishing the European Community, 25 March 1957, 298 U.N.T.S. 3., as revised in 10 Nov. 1997, 1997 O.J. (C340) 173 [hereinafter 'EC Treaty']. The basic standards of the EC Competition Rules are stated in Article 81 of the EC Treaty . That Article prohibits all agreements between undertakings that may affect trade between Member States and also prohibits all agreements which distort competition within the common market. Article 81 also states that its provisions may be declared inapplicable, in certain circumstances, by way of individual or block exemptions. [For more details, see Waelbroeck and Frigani *European Competition Law* (New-York, 1999)].

2 Decision of March 30, 1984, O.J. 1984 L 99/29 ("*Nuovo Cegam*"); Decision of December 5, 1984, O.J. 1985 L 35/20 ("*Fire Insurance*").

3 *Ibid.*

4 Case 45/85, *Verband der Sachversicherer e. V. v. Commission*, 1987 E.C.R. 405.

5 For a comparative view over the legal framework in selected states see U. Hübner, *Rechtliche Rahmenbedingungen des Wettbewerbs in der Versicherungswirtschaft* (Baden-Baden, 1st ed., 1988).

took place on the national level and was directed at national markets, at least as far as the Continent was concerned. Interstate trade was affected, if at all, only on a minor scale.

III. Special characteristics of the insurance industry

Turning to the *special characteristics* of the insurance industry, the traditional argument used to be that state regulation of the insurance industry can be justified for a number of reasons. All of which lead to the conclusion that state regulation is necessary, and that market forces and the competitive process cannot be relied upon. The same reasons justifying state regulation were, to some extent, also regarded as arguments why the general rules of competition law could not or should not be applied even-handedly and without exceptions to the insurance industry. This kind of thinking was reflected, for example, in the German law against restraints on competition: § 102 (in the 1973 version of the law) provided that the general prohibition on agreements and decisions restricting competition did not apply where the agreements and decisions were linked to matters which were subject to supervision by the Federal Supervisory Office for the Insurance Industry. The role of competition law was thereby restricted to questions constituting abuse of an existing market position.

1. There are essentially five so-called *special characteristics* of the insurance industry that are considered to legitimise state regulation and, at the same time, to justify a reduced role for competition law[6].

First, the *capacity argument*[7]: It is argued, that with regard to the production of insurance services, there are no material limits to the extension of insurance capacity and to market access as well. Insurance markets are supposedly characterised by excessive capacity and, hand in hand, with a downward tendency in premiums, leading to ruinous competition. Accordingly, unrestrained competition might lead to undesirable results.

Second, the *premium calculation* argument[8]: The insurance business has to rely on certain assumptions as to the realisation of risks in the future.

6 Critical as to these special characteristics W. Möschel in *Gesetz gegen Wettbewerbsbeschränkungen — Kommentar zum Kartellgesetz*, § 102 note 13–18 (München, 1st ed. 1981); Malitius in *Kommentar zum deutschen und europäischen Kartellrecht*, § 102 note 7 (Neuwied, 7th ed. 1994).

7 Cf. C. Hootz in *Gesetz gegen Wettbewerbsbeschränkungen und Europäisches Kartellrecht: Gemeinschaftskommentar* — §§ 102–102a GWB, § 102 note 8 (Köln, 4th ed. 1988).

8 *Ibid*, § 102 note 9; critical W. Müller & P. Zweifel "Deregulierung der Versicherungsmärkte durch die EG?" 40 *Wirtschaft und Wettbewerb* (1990) 907, 910–914.

In some sectors of the industry there is need for reliable statistics based on a broad number of insurance contracts. Small and middle-sized insurance companies, therefore, are often not able to rely on their own expertise[9]. The problem of uncertainty is encountered all the more often by companies which intend to enter the market, and in insurance branches where the contracts are generally concluded on a long-term basis. It is said that because of the lack of certainty in the calculation of premiums there is imminent danger that insurance companies, pressed by competition, will tend to underestimate the realisation of future risks. Thus, premiums would be calculated on a below-cost basis and, in the long run, lead to insolvencies which are a socially undesirable result. At least with regard to life and health insurance, insolvencies run counter to the very function of insurance as an instrument for long-term planning of future risks by individuals.

Third, the *transparency argument*[10]: Insurance products are products that the consumer, as a contract partner, finds hard to judge and compare, because they are usually defined by very complex policy conditions. Varying conditions may not be fully comprehended or even understood by the insured. All the less is the insured able to make an informed judgement on the product-premium relationship with regard to individual policy conditions. As policy conditions are easily changeable, there is no limit to product variations that, in the end, would lead to uninformed consumer choices as a result of lack of market transparency. Lack of transparency creates information problems that the consumer will often not be aware of, and also creates information costs the consumer will often not be willing to pay. In the end, competition on the product level is said to lead to undesirable results.

Fourth, the co- and re-insurance business heavily depends on *certain uniformity* of policy conditions and risk assessment in the direct insurance business, in order to keep transactions costs down[11].

Fifth, the *financial security* argument[12]: In order to be accepted by the general public, the insurance business depends on consumers' trust. Confidence in the financial stability of insurance companies is an essential precondition for the general public to use insurances as an instrument

9 S. Klaue "Zur Anwendung des europäischen Kartellrechts auf die deutsche Versicherungswirtschaft" *Betriebs-Berater* (1983) 2019, 2020.

10 *Ibid*, at p. 2020; Hootz, *supra* note 7, § 102 note 10; critical Müller and Zweifel, *supra* note 8, at pp. 914–916.

11 Hootz, note 7, § 102 note 11; cf. Siegfried Klaue, *supra* note 9, at p. 2020.

12 *Ibid*, § 102 note 12.

for planning the future. Insolvencies in the insurance sector may create intolerable social consequences for the insured, and might undermine public confidence in the insurance industry.

2. In its judgement of January 27, 1987 [13] the Court of Justice clarified the issue of applying the competition rules to the insurance sector in more than one respect: (1) It held, in what came for some as surprise, that trade among the member states might be affected by a contract between domestic insurance companies if out-of-state companies seated in other member states, participate in the agreement through their intrastate branches.

(2) The Court dealt with the "special characteristics" argument at length. Though Article 81 of the EC Treaty (ex-Article 85) [14] does not provide for an exemption for insurance, the insurer's association and the Federal Republic had argued that the Community competitions rules could not be applied to the insurance industry without restrictions and reservations on grounds of the "special characteristics" of the insurance contract. Both pleaded that there was an obligation on the Council to adopt special rules on the basis of Article 83(2)(c) of the EC Treaty, in order to temper the rigour of the prohibitions of Articles 81 and 82 of the EC Treaty. The argument was that as long as such rules had not been promulgated, the prohibitions contained in Article 81(1) of the EC Treaty could not be applied [15]. The Court rejected the contention that Community competition law provided for a special treatment of the insurance industry since neither the Treaty itself nor Regulation No 17/62 [16] provide exceptions, comparable to those available for agriculture (Article 36 of the EC Treaty) or land, sea, and air transport. However, the Court made expressly clear that Community competition law in no way prevents "special characteristics of certain branches of the economy to be taken into account" within the framework of Article 81(3) of the EC Treaty, the Commission having the power to grant exemptions from the prohibitions contained in Article 81(1) of the EC Treaty [17].

The *Verband der Sachversicherer* judgment set off a great number

13 *Verband der Sachversicherer e. V. v. Commission, supra* note 4, 1987 E.C.R.

14 Since the entry into force of the Treaty of Amsterdam, all of the articles of the EC Treaty have been renumbered. The numbering used throughout this article is compatible with the current version of the EC Treaty.

15 Cf. *Verband der Sachversicherer, supra* note 4, 1987 E.C.R. 405, 450 f. para. 8, 10; Bodo Börner, *Die vorläufige Nichtanwendbarkeit des Artikels 85 EWGV auf die Assekuranz* (Karlsruhe, 1984) at pp. 32–38.

16 Reg. 17/62 of February 6, 1962, O.J. 1962 p. 204.

17 Cf. *Verband der Sachversicherer, supra* note 4, 1987 E.C.R. 405, 451–52 para 15.

of notifications by insurance companies to the Commission (more than 300), creating a problem all too well known in the history of European competition law. After handing down two exemption decisions in 1990 (*"TEKO"; "Concordato Italiano Incendio"*), the Commission, empowered by Council Regulation No. 1534/91 [18], issued the Block Exemption Regulation No. 3932/92 of 1992 [19], exempting four different types of agreements and concerted practices from the prohibitions of Article 81(1) of the EC Treaty.

C. Horizontal agreements

Before going into the details of the Block Exemption Regulation a short description of the impact of the competition rules on the insurance industry shall be given. For reasons of brevity it will neither deal with the abuse of dominant positions (Article 82 of the EC Treaty) nor with the merger control regulation. In both areas, the insurance industry does not play a special role, nor is it treated in a special way.

I. General observations

1. Starting with *horizontal agreements*, two Commission Notices, that are of relevance to the insurance sector in the same manner as with regard to other sectors, have to be mentioned, for they give insurance companies considerable leeway for co-operation.

a) The new Commission Notice on agreements of minor importance of December 4, 1997 [20] has materially altered the "*de minimis*" ("appreciability") test, as applied by the Commission. The Notice abolishes the turnover test of the former Notice of 1986 [21], concentrating on the market share test as the sole and decisive criterion. With regard to "horizontal agreements" only those agreements in which the combined market shares of the companies involved transcends 5% will be considered as "appreciably" restricting competition [22]. There is one *caveat* to be made: the Notice states in its Sec. 11 that application of Article 81(1) of the EC Treaty "cannot be excluded" with regard to agreements that have as their object to fix prices, to restrict production or distribution (by quotas etc.) or to share markets. Such

18 Reg. 1534/91 of May 31, 1991, O.J. 1991 L 143/1.
19 Reg. 3932/92 of December 21, 1992, O.J. 1992 L 398/7.
20 O.J. 1997 C 372/13.
21 O.J. 1986 C 231/2.
22 Sec. 9 of the notice, *supra* note 20.

agreements are considered by the Commission as "*per se*" restrictions under Article 81(1) EC Treaty. As the Notice is also applicable to the provision of services, the 5% market share rule, and the above-mentioned exceptions are relevant for the insurance sector as well.

b) In its Notice on co-operation agreements of July 29, 1968 [23] the Commission deals with the notion of restriction of competition. The Commission takes the view that agreements "having as their sole object: a) an exchange of opinion or experience; b) joint market research; c) the joint carrying out of comparative studies of enterprises or industries; d) the joint preparation of statistics and calculation models", do not restrict competition and, therefore, are not caught by the prohibition of Article 81(1) of the EC Treaty. It is suggested that there is a considerable overlap between this Notice and the Block Exemption Regulation to be discussed below.

2. Besides the examples listed in the Commission Notice on co-operation agreements, there are, of course, other cases of co-operation that do not amount to restriction of competition. One example would be the ad-hoc-formation of a co-insurance co-operation between insurance companies that are not in a position to insure the relevant risk on their own [24]. Such co-operation may be regarded as competition-creating rather than competition-restricting, as long as the co-operation is devoted and limited to a single case [25]. A comparable argument can be made where the co-insuring companies sustain sufficient capacity, but co-insurance is organised on behalf of the customer who prefers to be insured by way of co-insurance rather than only by one single company.

On the other hand, Article 81(1) of the EC Treaty will apply to agreements on, or recommendations of commercial (gross) premiums, their concerted rise, minimum levels [26], maximum commissions to be paid to agents [27], the prohibition of rebates or discounts. To these agreements, the usual principles under Article 81(1) of the EC Treaty are applicable. The same holds true for market sharing agreements.

23 O.J. 1968 C 75/3, corrected in O.J. 1968 C 84/14.

24 Commission decision of April 12, 1999, No 66 ("*P&I Clubs*"), O.J. 1999 L 125/12.

25 Report of the Commission on the application of Reg. 3992/92 of May 12, 1999, Com (1999) 192 final, No. 25.

26 Cf. Commission decision of December 4, 1992, No 30–32 (*"Lloyd's Underwriters"*), O.J. 1993 L 4/26.

27 The later agreements may, however, be exempted under Article 81(3) of the EC Treaty; cf. Commission Notice pursuant to Article 19(3) of Reg. No 17 ("Insurance Agents"), May 6, 1987, O.J. 1987 C 120/5.

II. Block Exemption Regulation No. 3932/92[28]

Turning now to the 1992 Block Exemption Regulation issued by the Commission, the more technical problems, e.g. the scope[29] or the legal consequences of "overstepping" the block exemption[30], are left aside. The four types of arrangements that are, under certain conditions, exempted from the prohibition of Article 81(1) of the EC Treaty have to be addressed from the perspective of whether and to what extent the block exemption regulation takes care of the so-called *"special characteristics"* of the insurance sector.

1. Calculation of premiums

a) Articles 2–4 of the Regulation deal with co-operation in the calculation of premiums. In a nutshell, the regulation exempts all agreements that relate to (1) the calculation of the *average cost* of risk cover (i.e. pure premiums); (2) the establishment of *statistics* like mortality tables, tables on the frequency of illness, accidents, and invalidity, provided that the tables will be based on compilation of sufficient data in order to be handled statistically; (3) the carrying out of *studies* related to the probable impact of general circumstances on the frequency or scale of claims and on the profitability of different types of investment.

The calculation principles and the statistical material have to be treated and described as *purely illustrative*[31] and non-binding[32]. They may not be so specific as to enable competitors to identify certain insurance undertakings[33]. And finally, it is prohibited to include within the co-operation the collection of statistical information relating to overhead costs, such as commissions, adjustment and investigation costs, claims handling, staff costs, and the anticipated profits of the undertakings concerned[34].

b) The exemption takes care of what has been described as the *premium calculation* problem. Insurance companies with a relatively small number of

28 Reg. No 3932/92 of December 21, 1992, O.J. 1992 L 398/7. See the recently published Report of the Commission on the application of Reg. 3932/92 of May 12, 1999, COM (1999) 192 Final, and the position of the Economic and Social Committee, O.J. 2000 C 51/105.

29 See *Comité Européen des Assurances*, Cea Info, Special Issue no 2 — october 1993, Competition: adaption of European competition law to insurance 103–110 (1993).

30 Cf. A. Fitzsimmons *Insurance Competition Law* (London, 1994) 70–71.

31 Article 3 lit. a) of the Block Exemption Regulation.

32 *Ibid*, Article 4.

33 *Ibid*, Article 3 lit. c).

34 *Ibid*, Article 3 lit. b).

covered risks in a certain branch, as well as companies which intend to enter the market, face a competitive disadvantage vis-à-vis the larger companies that are in a position to develop the relevant statistical information based on their own business activities[35]. As far as co-operation is related to the calculation of pure premiums and to the development of statistical tables without any obligation to abide by them in the calculation of the commercial ("gross") premiums, one might argue that this form of co-operation does not even amount to restriction of competition[36]. It rather promotes the emergence of a "level playing field" and the thereby enhances the competetiveness of smaller insurevs[37].

The exemption appears to serve as an effective device to overcome the premium calculation problem for smaller insurance companies[38]. To the extent that the availability of the calculation and statistical material to all competitors leads to a somewhat higher degree of premium uniformity, such a restrictive effect may be considered as consequence of and justified by a better knowledge of the relevant statistical information. There can be no objection to that as long as there is no obligation nor any pressure whatsoever to calculate the premiums on the basis of the relevant data. Article 4 of the Block Exemption Regulation expressly withholds the benefit of the exemption for those companies or associations that impinge upon this principle.

2. Standard policy conditions

Articles 5–9 of the Block Exemption Regulation deal with standard policy conditions for direct insurance. The exemption covers agreements, recommendations etc., that have as their object the establishment and distribution of *standard policy conditions*[39] and of common models illustrating the profits to be realised from insurance involving a capitalisation element[40].

35 Cf. H. A. Schmidt, *Die Europäisierung des Kartellrechts im Bereich der Kredit- und Versicherungswirtschaft* (Baden-Baden, 1st ed., 1995) 132–133; see also Report of the Commission, *supra* note 27, No 6 and N. Paul and R. Croly, EC-Insurance Law § 13.18 (1991).

36 As set forth in the Commission's Notice on co-operation of 1968 ("joint preparation of statistics and calculation models"), *supra* note 23. See Position of the Economic and Social Committee, *supra* note 28, No. 3.1.

37 Cf. Report of the Commission, *supra* note 28, No. 6.

38 Cf. Fitzsimmons, *supra* note 30, at p. 75.

39 Article 5 sec. 1, *supra* note 31.

40 *Ibid*, Article 5 sec. 2.

Co-operation with regard to standard policy conditions is exempted only under three general conditions: (1) The standard policy conditions must be expressly described as purely illustrative, i.e. non-binding for the addressees, (2) they must expressly mention that different conditions may be agreed upon in the contracts with the insured, and (3) they have to be accessible to any interested person[41].

The Block Exemption Regulation contains a so-called *"black list"* of eleven clauses that must not be contained in model standard policy conditions. One main object of the black list is to make it clear to any insurance company that it may freely deviate from the standard conditions in its own policy conditions. It deals with clauses relating to the formulation of the insurance "product", the coverage of risks, the contract period, and the contractual rights of the insured.

The most important clauses are the following[42]: (1) Clauses that exclude from the coverage losses that are normally related to that class of insurance; clauses that include in the coverage losses that a group of insured is not exposed to; clauses that make the cover subject to specific (i.e. security) conditions. With regard to all those clauses there has to be an explicit indication that the insurer remains free to shape the insurance product in a different way[43]. (2) Indications as to the amount of the coverage, or as to the portion which the policy holder must pay himself, must be totally omitted[44]. (3) The insurer may not be given the right to restrict the scope of insurance coverage, to increase the premiums to be paid without a change in risk factors, to modify the contract period or to change the policy conditions without the express consent of the policy holder[45]. Moreover, the contract period must be no longer than three years (except in life insurance), and contract renewal periods may not be longer than one year in case that the policy is automatically renewed[46]. (4) The standard policy conditions must not contain "tying clauses", requiring the policy holder to obtain coverage from the same insurer for additional risks[47].

The exemption for standard policy conditions takes care of the *trans-*

41 *Ibid*, Article 6 sec. 1. lit.c).

42 Cf. Fitzsimmons, *supra* note 30, at pp. 77–82.

43 Article 7 lit. a)–c), *supra* note 31.

44 *Ibid*, Article 7 lit. d).

45 *Ibid*, Article 7 lit. e)–f).

46 *Ibid*, Article 7 lit. g)–h).

47 *Ibid*, Article 7 lit. j).

parency issue[48]. It leaves it to the insurance industry to develop somewhat homogenous products, without preventing product innovation[49]. The Commission expressly justifies the exemption with the argument that standard policy conditions and standard individual clauses "have the advantage of improving the comparability of cover for the consumer"[50]. At the same time, they enable to classify the risks more uniformly so that reliable statistical material can be developed[51].

The Commission has been harshly criticised for the far-reaching exemption for standard policy conditions. The main argument was that the exemption might lead to less product variety than is desirable for the consumer[52]. In my opinion, a more optimistic appraisal of the group exemption should be made. The standard conditions have a wholly illustrative, non-binding character. On this basis, product innovation may take place at any time, either on demand of individual consumers or on demand of consumer interest organisations[53]. Compared to the German system of pre-market regulation of policy conditions, which existed until 1994, the exemption for standard policy conditions in the Block Exemption Regulation seems to achieve a fair compromise between the somewhat conflicting aims of transparency with regard to policy conditions, comparability for the consumer of the relevant product/premium relationships, and product variety, without excessively discouraging product innovation.

The *"black list"* catalogue in Article 7 of the Block Exemption Regulation has been strongly criticised for still another reason. The criticism contends that a number of clauses on the black list are directed towards *consumer*

48 Cf. H. J. Bunte, Eine Gruppenfreistellungsverordnung für die Versicherungswirtschaft, 42 *Wirtschaft und Wettbewerb* (1992) 893, 900–901; Paul and Croly, *supra* note 35 at § 13.21 (1991).

49 M. Adel "Deregulierung der Versicherungswirtchaft durch die Gruppenfreistellung der Europäischen Kommission" 83 *Zeitschrift für die gesamte Versicherungswissenschaft* (1994) 77, 90–91.

50 Ground No. 7 of Reg. 3932/92.

51 Cf. C. Hootz, *Gesetz gegen Wettbewerbsbeschränkungen und Europäisches Kartellrecht: Gemeinschaftskommentar, EG-Gruppenfreistellungen — Branchen-Regelungen: Versicherungswirtschaft*, Article 5 note 1 (4th ed., 1996).

52 Müller and Zweifel, *supra* note 8, at pp. 914–916; the argument, however, seems to be based on the assumption that the insurers are obliged to use the model conditions in their business.

53 Hootz, *supra* note 51, at Article 6 note 1; Adel, *supra* note 49, at pp. 90–91.

protection, and not towards *competition policy*[54]. This claim is made especially with regard to provisions such as that requiring that a contract period of more than three years will not be imposed, or that the renewal period may not be longer than one year where the policy is automatically renewed, or that the contract period can be changed by the unilateral decision of the insurer. Provisions like the above cited undoubtedly have a strong consumer protection flavour. This does not mean, however, that the Commission lacks competence to deny exemption from model conditions that contain "black list" clauses at least for two reasons. First, an exemption from the prohibition of Article 81(1) of the EC Treaty can only be granted if — in the language of Article 81(3) of the EC Treaty — consumers are allowed "a fair share of the resulting benefit". Though Article 81(3) of the EC Treaty does not grant the Commission competence to actively pursue a consumer protection policy under the disguise of competition law, it is under the duty to vigorously ensure that the co-operation between insurers in formulating standard policy conditions will not lead to apparent disadvantage for the consumers. Thus, the Commission cannot escape its duty to give the consumers their "fair share"[55]. Second, the "black list" clauses do not relate to the product/premium relationship or to the equities between the parties, but to the freedom of the consumer to rescind the contract and his/her freedom to switch — after a certain time span — to another insurer. All the relevant clauses relate to this freedom of selection[56] and are thereby intrinsically related to competition between insurance companies. Freedom of the insured to change the contract partner makes market access easier, and tends to make product innovation more profitable. Consumer protection and the protection of the competitive process are just two sides of the same coin in this respect[57].

3. Security devices

The Block Exemption Regulation applies to agreements and recommendations that have as their object the creation, recognition, and distribution of

54 Hootz, *ibid*, at pp. 85–86.

55 Cf. F. von Fürstenwerth, "EG-Gruppenfreistellungsverordnung für die Versicherungswirtschaft", (1994) *Wertpapiermitteilungen* 365, 369.

56 Cf. G. Vernimmen, *"Die Gruppenfreistellungsverordnung für die Versicherungswirtschaft"*, (1993) *Versicherungswirtschaft* 559, 560; Fürstenwerth, *ibid*, at p. 369.

57 See also W. Veelken, in *EG-Wettbewerbsrecht*, vol. I, GFVO H. note 7 at p. 653 (München, 2nd ed., 1997).

technical specifications, procedures for assessing and certifying compliance with such specifications, and rules for the evaluation and approval of installation undertakings[58].

This exemption is not particularly related to one of the "special character istics" discussed above. It rather builds on the Community's 'new approach' in the field of technical harmonisation and standardisation of 1985 that is meant to improve the functioning of the internal market, the assumption being that uniform standard quality criteria throughout the Community will promote competition[59]. The relevant agreement is exempted under certain conditions set forth in Article 15, the most important being the non-binding and non-discriminatory character of the agreement, the accessibility of the specifications to interested persons, their transparency, objectivity, and proportionality.

The exemption relates to the justification of the "promotion of technical and economic progress", as set forth in Article 81(3) of the EC Treaty. It is submitted that technical specifications and standard certifications as to security standards tend to simplify risk classification, thereby reducing transaction costs. Given their non-binding character, the insurance undertakings shall be free to accept other security devices as well[60]. To that extent, the exemption serves a useful purpose without being overly restrictive.

4. Common coverage of risks

A fourth exemption in the Block Exemption Regulation concerns agreements that have as their object the setting-up and operation of groups of insurance undertakings for the common coverage of certain categories of risks in the form of co-insurance or co-reinsurance[61].

a) Scope of application

As mentioned before, co-operation by way of co-insurance is not necessarily covered by Article 81(1) of the EC Treaty: Where co-insurance is organised for the coverage of a single risk, where insurance companies would encounter capacity difficulties operating individually, or where the contract partner (the insured) prefers coverage of the risk by way of co-insurance, the

58 *Supra* note 31, Article 14.

59 Cf. ground No 15 of Reg. 3932/92; Report of the Commission, *supra* note 28, No. 34–35.

60 Cf. Article 15 lit. c), *supra* note 31.

61 *Ibid*, Article 10 sec. 1.

preconditions to apply Article 81(1) EC are not fulfilled[62]. In contrast, Article 81(1) EC is likely to become applicable when insurance companies carry on the business of co-insurance on a regular basis for an undetermined number of risks.

b) Preconditions of exemption

Agreements with the object of setting up and operating groups of insurance companies[63] for the common coverage of specific risks will be considered exempted only if the market share of the group does not exceed 10% of the market share (with regard to "co-insurance groups") or 15% (concerning "co-reinsurance groups") of any of the markets concerned (i.e. "relevant market"). As to the potential group effect among the members of the co-insurance group, the market share in the relevant product market[64] is calculated by adding together the business transacted by the group itself and by the individual insurers[65].

With regard to special risks — e.g. catastrophe risks, where claims are both rare and large, or aggravated risks, which involve a higher probability of claims because of the characteristics of the risk insured — where the group effect is less likely to appear, the calculation of the market share has to be confined to the figures of the group itself[66].

c) Exempted provisions

The Block Exemption Regulation comprises a list of *"white"* clauses that may generally be regarded as not restricting competition. They relate to the nature and characteristics of the risks covered, the conditions governing admission to and withdrawal from the group, rules governing the operation management of the group, and rules on the individual own-account shares ("Selbstbehalt")[67].

The most important restriction which is exempted by Article 10(2) relates

62 Cf. Veelken, *supra* note 57, note 62 at p. 669; M. Schümann, *Die Gruppenfreistellungsverordnung 3932/92 für die Versicherungswirtschaft* (Frankfurt am Main, 1998) at pp. 164-167, (expect for insurance of a single risk); Bunte, *supra* note 48, at p. 902; see Schmidt, *supra* note 35 at pp. 159-163 (1995). See also Report of the Commission, *supra* note 28, No 25.

63 Defined in Article 10 sec. 2 lit. a) and b), *supra* note 31.

64 Cf. *ibid*, Article 11 sec. 1 lit. a): "Insurance products that are identical or regarded as similar from the point of view of the risks covered and of the cover provided".

65 *Ibid*, Article 11 sec. 1.

66 *Ibid*, Article 11 sec. 2.

67 *Ibid*, Article 10 sec. 3.

to the obligation to underwrite a specified risk category exclusively in the name of and for the account of the group, or to entrust the underwriting to a common broker or a common body set up by the group.

Co-insurance groups have to operate with some degree of uniformity vis-à-vis the insured as well as the re-insurer. For this reason, the Regulation exempts the obligation to use general or specific insurance conditions accepted by the group, to use commercial ("gross") premiums set by the group, to submit to the group for approval the settlement of claims relating to co-insured risks, to entrust the group with the negotiation of re-insurance agreements on behalf of all concerned, and the obligation not to re-insure the individual share of the co-insured risk[68].

d) The justification of the exemption

The exemption for the common coverage of certain risks relates to the "special characteristics" discussion undertaken insofar, as it is contended that the business of co-insurance heavily depends on a certain degree of uniformity of policy conditions and premiums alike[69]. Before issuing the Block Exemption Regulation the Commission had gained some experience as to insurance pools. In its *Nuovo Cegam*[70], *P & I Clubs*[71], *TEKO*[72] and *Assurpol*[73] decisions, it has taken an approach that has been described as "much more realistic as to the genuine difficulties which are encountered by small or inexperienced insurers and re-insurers..."[74] in connection with risks that are either novel or involve infrequent or catastrophic losses. The favourable attitude of the Commission towards co-insurance is reflected by the following statement in ground No 10 of the Block Exemption Regulation: "The establishment of co-insurance and co-/re-insurance groups designed to cover an unspecified number of risks must be viewed favourably insofar as it allows a greater number of undertakings to enter the market and, as a result, increases the capacity for covering, in particular, risks that are difficult to cover because of their scale, rarity or novelty". Though the limits to this justification are not reflected in the exemption of the Regulation, it

68 *Ibid*, Article 12; for special provisions concerning co-/re-insurance groups see Article 13.
69 Cf. Schümann, *supra* note 62, at p. 178.
70 Decision of March 30, 1984, O.J. 1984 L 99/29.
71 Decision of December 16, 1985, O.J. 1985 L 376/2.
72 Decision of December 20, 1989, O.J. 1990 L 13/34.
73 Decision of January 14, 1992, O.J. 1992 L 37/16.
74 Fitzsimmons, *supra* note 30, at p. 84.

is suggested that the Commission has, indeed, taken a balanced approach to the necessities of co-insurance, making sure that the exempted groups of insurers may not be able to gain appreciable market power. In its *TEKO* decision [75], the Commission has stressed its assumption that in the area of specialized risks, where only a small number of contracts will be concluded by each individual insurer, the framework of co-insurance may lead to substantial rationalisation and cost savings. The individual company may gain specialised experience required for the conclusion of such contract, and the group of insurers may be able to negotiate more favourable terms and conditions vis-à-vis the re-insurer. Given the rather low market share figures of 10% (or 15%) comprising the business of the group and the individual members, it is fair to assume that only rather small groups will benefit from the exemption, whereas larger groups will still need an individual exemption by the Commission. It may therefore not come as a surprise that criticism of the low market shares has been lodged by representatives of the insurance industry [76]. This can be taken as an indication that the Commission's approach should be perceived as a rather cautions one. [77]

III. Individual exemption decisions

It goes without saying that in case of an agreement not covered by the Block Exemption Regulation, i.e. in the case of "overstepping", an individual exemption decision by the Commission may be applied for. This relates, inter alia, to co-operation in the handling of damage claims or the setting up of re-insurance groups. A further example relates to the Commission Notice (*"Insurance Agents"*) [78], persuant to Article 19(3) Regulation 17/62. In this notice the Commission indicates that it is ready to exempt agreements on maximum commissions to be paid to agents with regard to the cost savings encountered by the insurance companies and the advantages for consumers resulting from lower premiums.

75 *Supra* note 72.
76 Cf. Von Fürstenwerth, *supra* note 55, at p. 372.
77 Cf. as to the three step analysis of the Commission Report of the Commission, *supra* note 28, No. 28–31.
78 O.J. 1987 C 120/5.

D. Vertical restrictions

With regard to vertical restrictions, the *general principles* of European competition law apply without any discernable influence of the so-called "special characteristics" discussion. Therefore, a few remarks will be sufficient.

1. In its Notice pursuant to Article 19(3) Regulation 17/62 (*"Standard Life/Halifax"*)[79], the Commission dealt with an *agency agreement* between Standard Life Assurance Co., the 2nd largest British life insurance business (4th in Europe), the tenth largest business in the British insurance market, with a market share of 6%, and Halifax, the largest building society. Building societies represent important channels for the distribution of assurance products. In 1987 they accounted for 18% of sales of non-linked assurance products. In 1990 some 94 building societies with approximately 7,000 branches were tied to insurance companies as exclusive agents, leaving 14 building societies with some 955 branches (which accounts for 14% of the total) to act as independent financial advisors. Halifax was to be appointed as a representative and therefore, under English law, exclusively working for Standard Life. The agency agreement contained a prohibition on Standard Life to appoint competing building societies as representatives besides Halifax. Given the special position of a building society as an appointed representative, it is acting in two markets (the retail investment product market of its principal and the distribution of its own investment products). As a result, there is the danger that competition on the market of investment products would become distorted and that Halifax, as the sole representative, may gain a competitive edge over competing building societies, taking advantage of the standing of its principal as leading assurance company. On this basis, the Commission refused to exempt the relevant clause under Article 81(3) of the EC Treaty.

2. The Commission's Notice in the matter of *Standard Life/Halifax* also concerns a contractual *prohibition on commission rebating*. Such a prohibition works in effect like a vertical price-fixing agreement as it prevents the representative from actively engaging in price competition by reducing their own profit margin.

A prohibition to offer customers a rebate or discount of one's commission may also be introduced by state regulation. In the "*Meng*" decision of November 1993[80], the Court of Justice upheld such a regulation against

79 O.J. 1992 C 131/2.

80 Case C-2/91, *Meng*, 1993 E.C.R. I-5751, 5797–98 para 14–22.

the claim that it infringes Articles 10(2) and 81(1) of the EC Treaty. In contrast, a contract will fall under Article 81(1) EC if a comparable clause is included, provided that competition is appreciably restricted. Thus, in the "*Standard Life*" Notice the Commission denied an exemption under Article 81(3) of the EC Treaty from a prohibition on commission rebating[81]. It should be noted that with regard to vertical agreements the Commission Notice on agreements with minor importance assumes an appreciable effect at the threshold figure of 10% of the market share, but excluding agreements that have as their object the maintenance of resale prices.

3. As far as I can see, the Commission has not yet dealt with *long-term contracts* and their potential effect on competition as a question of vertical restrictions. Whereas in some national markets, the vast majority of insurance contracts at least with commercial customers, are concluded and/or renewed on a yearly basis, the practice in other Member States tends towards insurance contracts for longer periods. From the perspective of competition law, long-term insurance contracts seem to be problematical insofar, as they may, if widespread, have a restrictive effect on market access[82].

Article 81(1) of the EC Treaty will only be applicable if the insured is an "undertaking" and not a non-commercial consumer. Moreover, a single long-term contract will, of course, never have an appreciable effect on competition. The Court of Justice, in its "*Henninger Bräu AG*" judgment has called for a full-fledged analysis of the relevant market: the potentially cumulative effect of contract networks on access to the market, the very characteristics of the market (whether saturated etc.) and the potential alternatives for new competitors to penetrate the bundle of contracts[83].

It should be noted that restrictive practices on the distribution level, e.g. beer distribution as in "*Henninger Bräu*", may have a different impact on market access as compared to de facto restrictions vis-à-vis the demand side or the final consumer. Restrictions on access to the distribution level may perhaps be overcome by strategies of vertical integration or by developing or using other distribution channels, whereas foreclosure on the final demand side level — as is achieved with long-term insurance contracts — cannot be

81 As to agreements on maximum provisions, see K. Schumm in *Kommentar zum EU-/EG-Vertrag*, vol. 2/I, Artikel 85 — Fallgruppen Versicherungen, (5th ed., 1999) note 50 at p. 718.

82 Cf. T. Entzian, "Versicherungsverträge und europäisches Kartellrecht", (1996) *Zeitschrift für Europäisches Wirtschafts — und Steuerrecht*, 342, 343–344, 347–348.

83 Case C-234/89, *Delimitis v. Henninger Bräu*, 1991 E.C.R I-935, 984–987, para 16–27.

overcome by companies that seek to enter the market. Nevertheless, I would suggest that the evaluation of long-term contracts is a matter falling rather under Article 82 of the EC Treaty — abuse of a dominant position — than under Article 81(1) of the EC Treaty. The length of insurance coverage by a contract is an essential feature of the very product that is defined and offered by the insurance company. Because the time length is a matter of product definition, it should generally not be treated as a restriction of competition.

E. Conclusion

I would like, by way of summarising, to take another look at the relationship between European competition policy and those features that have been described as "special characteristics" of the insurance industry. A somewhat closer look reveals that there exists a kind of division of roles between competition policy and regulation policy.

1. Though financial security of insurance companies is a commonly accepted aim of "prudential regulation", it is mainly under the responsibility of the competent authorities of the home state of the insurance company concerned. Supervision takes place as post-market control with only indirect influence on the calculation of premiums and with nearly no influence on the formulation of policy conditions. European competition policy is directed at safeguarding the financial security of insurance companies only insofar as it gives the industry some leeway for gathering statistical materials and calculating premiums on the basis of average costs of the risk covered.

2. The aim to promote uniformity of policy conditions in order to facilitate co- and re-insurance and to improve transparency for the consumer is no longer a justification for state regulation. However, insurance undertakings may, by way of co-operation, develop non-binding model conditions that may — if used by the insurers — promote uniformity, at least to some extent, without sacrificing product innovation. Model conditions may tend to promote transparency and thereby comparability between the products of competing insurance companies.

3. European competition policy gives some leeway for gathering statistical material and calculation of average cost of risk coverage. This leeway is to some extent related to the financial security aim, but it also promotes competition by making information available to smaller insurance companies and companies that wish to enter the market.

4. The capacity argument is addressed by insurance supervision ("prudential regulation"), especially by capital and solvency requirements, not by European competition policy.

5. In sum, European competition policy is much more pro-competitive than its traditional German counterpart. It is based on a reasonable leeway given to the insurance industry to co-operate on certain issues, without endangering the competitive process. The claim that in the last 15 years anti-competitive Member State regulation has just been replaced by an anti-competitive autonomy for industry self-regulation appears to be one-sided . It needs to be replaced by a more differentiated and favourable appraisal.