Position Paper

EICL - Insurance Europe's response to Discussion Paper II

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Summary

Insurance Europe welcomes the opportunity to comment in writing on Discussion Paper II, forming the basis of discussions during the second meeting of the expert group on European insurance contract law (EICL) (held on 15-16 May 2013), and the relevant section of the final report that will represent the work-output of the expert group by the end of 2013.

Introduction

Insurance Europe maintains its continuing wish to assist the European Commission in its work of the expert group - set up to establish whether contract law obstacles exist that hinder the cross-border provision of insurance and, if so, establish in what areas of insurance such obstacles are most prevalent.

However, Insurance Europe does have some concerns arising from the organisation of the expert group and the possible publication of working materials arising from its work. There also remains concern over the scope of the work of the expert group – in particular the danger of straying into areas either beyond *contract law*, or into topics forming the basis of on-going discussions within the EC institutions (such as, for example, PRIPs and IMD2). Lastly, Insurance Europe has yet to receive evidence that differences in contract law represent the main obstacle to cross-border insurance provision.

Overarching comments

Organisation

Insurance Europe remains **concerned that the timeframe set aside to conduct this detailed exercise could jeopardise the accuracy and relevance of the outcome of the work** of the expert group, especially where the work of the group exceeds its mandate. In particular, there is a real risk that the input the European Commission seeks, and the timeframes permitted to collate and develop responses between meetings, compromises the ability of the European insurance industry, through this federation, to be as constructive as is desired by the industry.

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Scope of work

Secondly, Insurance Europe is **concerned to see that several issues already being discussed within the European institutions are referred to within the material for the work of the expert group**. In particular, *pre-contractual and contractual provision of information* and *advice* in relation to the purchase of insurance products should not be addressed in detail within this group, and should respect the continuing work of the European institutions on topics such as "packaged retail investment products" (PRIPs) and the revised insurance mediation directive (IMD2) by not anticipating the outcome of the discussion on PRIPs and IMD2. The complex issues that arise in relation to these topics and any discussion thereof, the cross-over of issues and the protection of stakeholders affected by these initiatives should reflect the outcome of the on-going legislative procedures.

The issue of *advice* should similarly not be discussed within the expert group's work as a *contract law* issue. In some member states, insurance products can be sold on either an *advised* or a *non-advised* basis. This flexibility in distribution methods should be safeguarded as it benefits the consumer by enabling access to insurance products that might otherwise have been inaccessible by some consumers due to, for example, the costs of advice. This flexibility also benefits the insurer by maximising the methods of distribution of its products. It is not a contract law issue as such and in any event is under on-going discussion within the European institutions.

Insurance Europe would reiterate the importance of ensuring that the objectives of the expert group (as set out by the European Commission) are met, namely:

- To explore whether differences in insurance contract law pose an obstacle to cross-border trade in insurance products, and
- If so, to identify the insurance areas which are likely to be particularly affected by such obstacles.

These are matters of objective assessment and the expert group's work should therefore be evidence-based. The expert group should concentrate on issues directly relevant to attaining these objectives and should avoid being distracted by other considerations. For example, it is not required to deliver an opinion on whether or not an "additional supra-national law" is, in itself, a desirable objective of EU policy or otherwise identifying "solutions" – the mandate is an evidence-based, fact-finding exercise to assess whether there are contract law obstacles to cross-border provision of insurance products.

Lack of evidence

Thirdly, **it remains unclear whether there is any evidence to suggest that a cross-border insurance market**, particularly in respect of mass risks, **would develop** if differences in contract law that may currently cause obstacles to such provision were overcome. It also remains uncertain, for lack of evidence, whether there would be sufficient demand to overcome and warrant the inevitable business costs associated with the supply of cross-border insurance products. Therefore, there is as yet no evidence that consumers, businesses or insurers would benefit substantially from any attempt to address differences in national contract law provisions which may be identified by this expert group as causing obstacles to the supply of cross-border insurance.

The mere fact that there is less insurance provision cross-border under freedom of services provisions (FOS) than, say, freedom of establishment (FOE) does not mean that a market should or would be created by removing possible contract law obstacles. Several factors affect insurers' decision to offer insurance cross-border. These include important factors such as 'knowing your customer', understanding the true risk proposed for cover (which will necessitate a thorough understanding of the applicable law, local legal interpretations in the courts, the interaction between different branches of law, and customs), language, culture (including expectations of the local policyholder), the form and prevalence of fraud, the tax environment and supervisory environment.

Likewise, there is no certainty that consumers would willingly take up cross-border products even if particular contract law obstacles identified by the expert group were removed and insurers were offering cross-border insurance provision on a broad scale. Several factors come into play for consumers considering their preferred service provider, including knowledge and expertise, reputation, pricing levels, service levels and so on of the insurance provider.

Discussion Paper I (in preparation of the meeting of the expert group that took place on 17-18 April 2013) references the Retail Insurance Market Study delivered to the European Commission in 2009 by Europe Economics. The Study's work on demand-side factors is pertinent to assessment of whether differences in insurance contract laws really constitute obstacles to cross-border trade in insurance. The Study cites a survey of 29,000 consumers in 25 member states as highlighting that consumers are mostly satisfied with domestic insurance offerings and concludes that latent demand for cross-border trade in insurance is likely to be low. This implies that differences in national insurance contract laws are unlikely to make a significant difference to customers' purchase of cross-border insurance and that therefore the extent to which they really act as obstacles to such cross-border activity is limited.

Additionally, the mere fact that there is a difference in national contract laws does not mean that contract law differences pose a problem and deters insurers from offering their products cross-border or makes it more difficult for them. Many important factors affect the decision to offer, or refrain from offering, insurance services cross-border (see above). Differences in contract laws represent only a minor aspect of the totality of obstacles considered and weighed up by insurers when considering whether to offer cross-border insurance within the internal market.

Detailed responses to questions contained in Discussion Paper II

Discussion Paper II, Section I, Question	Insurance Europe response
1.	Differences in national insurance contract laws play only a minor role in the supply of cross-border insurance of **large risks**. This is largely due to the bargaining position of the parties involved and the parties generally understanding their insurance needs and the nature of the contracts. The main reason for the relatively minor impact of differences in national contract laws on cross-border insurance provision of **large risks** is due to the parties' ability to negotiate and choose the relevant law (and jurisdiction) to apply to the insurance contract and, to a lesser extent, the application (by choice and custom) of supra-national conventions. MAT insurance – the insurance of ships (damage and liability), aircraft (damage and liability) and goods in transit - is an important segment of large risk insurance. The insurance market for these risks is international and by definition entails cross-border trade in insurance. MAT risks associated with EU member states constitute part of a larger, global whole and arrangements for their insurance do not differ substantially from those for the insurance of non-EU risks. MAT risks are often insured using the same policy forms whatever the risks' national origin. There is no evidence of problems with the supply of MAT insurance products: indeed, the markets are frequently characterised by over-capacity and an excess of insurers willing to provide cover. It is therefore reasonable to assume that differences in national insurance contract laws have little or no impact on the insurance of MAT risks. Similar considerations apply to the insurance of large non-marine risks (property and liability).

	Very large non-marine risks are often placed internationally on a subscription basis, by insurers based in more than one EU member state. Again, this necessarily entails cross-border trading. Differences in the insurance contract laws of EU member states are not an important consideration in this process.
2.	The parties to contracts insuring **large risks** make widespread use of the possibility to choose the applicable law. In some instances, this is done on the basis of Rome I, Art. 7(2), but it is not very common and is in general only done if the insurer has no legal entity in the host state. In some markets it is more common to cover large risks by international insurance programs, where there is a so called master policy and local policies covering local risks. Differences may arise depending on the type of insurance (for instance engineering lines or goods in transit/marine insurance). It is not possible to state the preferred choice of law in cross-border insurance contracts for **large risks**. This will depend on the contract in question and will be an element of the negotiation between insurer and policyholder. The London market is one of the leading providers of MAT insurance. Most of the MAT contracts underwritten in this market are subject to the laws of England and Wales, irrespective of the location of the insured. English law has an extensive body of judicial decisions on insurance disputes and a substantial library of scholarly writings on the subject. English law on marine insurance was codified in the Marine Insurance Act 1906, which is the basis for the marine insurance laws of other countries worldwide. The market uses policy terms and conditions that have been drafted with English law in mind and sometimes have been the subject of court decisions. In addition, there is a large legal sector in London experienced in advising on insurance law. Consequently, choosing English law can provide legal certainty to the parties to an MAT insurance contract. The purchasers of **large-risk** insurance are often large commercial enterprises with access to insurance experience both in-house and from the insurance broking sector. Agreement by such purchasers to the law applying to the contract is an informed decision. Courts inside and outside the EU are usually prepared to recognise such choices (e.g. the US Supreme Court decision in M/S BREMEN v. Zapata Off-Shore Co., 407 U.S. 1, 15 (1972)). Nevertheless disputes sometimes arise, generally because the choice of law has not been clearly documented. In the London Market, for example, insurance is usually placed on the open market Market Reform Contract, a standard template for the provision of information by brokers to insurers. This includes a mandatory field "Choice of law and jurisdiction", whose completion should reduce the chances of misunderstandings. Should the Commission require further information on other leading MAT markets, this can be provided separately.
3.	International markets for large risk insurance are relatively open to the introduction of new capacity. Such capacity is driven by the search for profits and is heavily dependent on the state of the market. It is not affected by issues such as differences in insurance contract law within the EU. The EU's legal framework for insurance, as set out in insurance directives, makes it reasonably easy for EU insurance undertakings to carry on business from other member states on either a services or an establishment basis. It therefore encourages EU insurers to carry on such insurance. An EU insurer considering whether to enter the **large risk** insurance market will consider very carefully whether this is likely to be profitable long-term. This will entail assessment of a range of factors: the ability to choose the law applicable to contracts may be a positive

	feature, but is very unlikely to make a material difference to the insurer's business strategy. Nor will it affect decisions on whether to carry on business on a services or establishment basis.
4.	Differences in national insurance contract laws may have some impact on the supply of insurance of **mass risks** cross-border, however, other more important factors than contract law differences affect insurers' decision to offer (or not to offer) such insurance contracts. These other factors include 'knowing your customer', understanding the *true* risk proposed for cover (which will necessitate a thorough understanding of the applicable law, local legal interpretations in the courts, the interaction between different branches of law, and customs), language, culture (including expectations of the local policyholder), the form and prevalence of frauds (particularly in respect of motor insurance), the tax environment (particularly in respect of private pension products) and supervisory environment. Although Rome I, Art. 7, sets out limits on the ability of parties to an insurance contract to choose the law applicable, it allows member states to grant greater freedom of choice of law. It would be helpful to understand which member states have done this and whether it has affected the provision of mass risk insurance within those member states on a cross-border basis.
5.	According to our experience the choice of law is an exception for **mass risks**. This may be influenced by the fact that clients are often focussed on their well-known national law and insurance conditions. As mass risks are subject to standardised processes an insurer will tend to apply only one contract law to its mass risks. Insurers will generally tend to offer insurance contracts, including for **mass risks,** in markets where they understand the risks to be insured so that they are able to accurately price their products in reference to relevant actuarial data. Insurers will also want to take account of both the business environment (for example the legal, tax and supervisory environment) and other factors (such as local culture, language, customs and customer expectations) that may affect the insurance contract. Insurers will also want to ensure they are able to establish a network to service the insurance contracts in accordance with their business needs and reputational objectives. The appropriate servicing of the contract before and throughout its duration, and the ability to manage claims arising from the contract (including providing additional assistance to policyholders) will have an impact on the decision to offer cross-border insurance of **mass risks**. EU insurers must also take into account the General Good provisions of other member states in which they offer insurance products. These often include detailed insurance contract law provisions. Although General Good measures are supposed to meet criteria laid down in the Commission Interpretative Communication on Freedom to Provide Services and the General Good in the Insurance Sector, it may be doubted whether all or even most do so. Therefore, although insurers may choose to supply insurance products cross-border, which in the case of **mass risks** will tend to be subject to the law of the host member state, the above factors will be the main obstacles to be overcome. Relative to these factors, the contract law applicable plays a minor role in the decision.
6.	Insurance Europe is not aware that the current EU legal framework on choice of law in cross-border insurance contracts for **mass risks** poses an obstacle to the supply of such contracts. This is because other factors such as language, culture, 'knowing your customer', local customs, and legal-, tax- and supervisory environments are likely to have a greater impact on the decision to provide cross-border insurance of **mass risks** than the ability to choose the law applicable to the contracts. Some EU non-life insurers do carry on **mass risk** business on a cross-border basis. Rather

	than trying to sell the same contracts as they provide in their home state, they may work with insurance intermediaries in the host member state to offer insurance contracts that are in line with the expectations of local customers. Often the contracts will be subject to the law of the host member state, which is usually the member state where the risk is situated and the policyholder has his habitual residence. Not only does this comply with Rome I, Art. 7, it is generally in line with customer expectations. Making the contract subject to the law of, say, the insurer's home member state would mean that, in the event of a dispute, the customer would either have to bring a legal case in the insurer's home member state, which is likely to be a costly process, or a court in the host member state would deliver a ruling based on the law of another member state, probably an unsatisfactory procedure. This is likely to affect the ability of the insurer to sell the product. So the choice of local law to govern a contract is not just a matter of legal compliance, but has a commercial motivation as well. There are some cross-border contracts where this does not apply, for example, the insurance of holiday homes, where the policyholder may be resident in a different member state from that in which the insured risk is located. If the policyholder is resident in the same member state as the insurer, they may prefer the contract to be subject to the home-state law. Such contracts make up only a negligible proportion of total EU property insurance. It is not possible for Insurance Europe to quantify any additional costs arising. The choice between FOS and FOE will in large part be a reflection of the factors raised in the response to question 5 above.
7.	Please refer to the response to questions 5 & 6 above.
8.	Insurers do adapt their contracts to the requirements of the member states where they operate, as they want to ensure that they comply with applicable legal and regulatory requirements. As noted earlier, adaptations to local contract law requirements are only a minimal element of the work necessary to underwrite risks situated in other member states successfully. Insurance Europe is unable to provide data quantifying the time and cost of adapting insurance contracts to local markets, in instances where insurers operate in more than one member state.
9.	The supply of mandatory insurance products is mainly affected by national liability regimes. This is particularly the case in respect of motor third party liability insurance. Additionally, obstacles like marketing, language, distribution and necessary adaptations to IT-systems play a role in the cross-border supply of mandatory insurance products. Existing differences in national insurance contract laws have a negligible effect on the supply of mandatory insurances. Some mandatory insurance products are, nevertheless, provided on a cross-border basis.
10.	Please refer to the response to question 6 above, substituting references to "mass risks" with "mandatory insurances".
11.	Please refer to the response to question 7 above, substituting references to "mass risks" with "mandatory insurances".
12.	Please refer to the response to question 8 above.

13.	It would appear that the cross border provision of insurance contracts for large risks is easier due, in part, to the likely sophistication of the policyholders seeking cover, while the cross-border provision of insurance for mass risks and mandatory insurances encounter greater obstacles due to the larger body of national (and international) legal provisions aimed at protecting the interests of less sophisticated policyholders and affected third parties (in the case of mandatory insurances and liability insurances).

Discussion Paper II, Section II, Question	**Insurance Europe response**
1.	Defining the term "insurance contracts" remains the biggest obstacle to the analysis of whether contract law obstacles affect the provision of cross-border insurance. Separate from pure national contract law provisions, national "general good rules" may also in some instances be used to discourage cross-border provision of insurance into a member state.
2.	The extent to which a particular aspect of national contract law impacts the provision of cross-border insurance will vary between member states and from insurance product to insurance product. In the event that identified contract law obstacles were resolved, a host of other important factors would remain that impact the provision of cross-border insurance contracts. These other factors include 'knowing your customer', understanding the true risk proposed for cover (which will necessitate a thorough understanding of the applicable law, local legal interpretations in the courts, the interaction between different branches of law, and customs), language, culture (including expectations of the local policyholder), the form and prevalence of frauds, the tax environment and supervisory environment. For example, the provision of certain private pension products will depend on the relevant tax regime in place. Similarly, studies have found that consumers in some member states prefer national insurers as they are more trusted than foreign insurers that may not have previously had a presence in the market. Such consumer bias is unlikely to be overcome merely by addressing possible contract law obstacles. Insurance Europe is not able to provide details quantifying the additional costs arising from differences in particular aspects of national contract laws.
3.	Where insurers wish to provide cross-border insurance this is likely to be offered through branches and thus via FOE. This is due to factors other than differences in national contract laws as set out in detail in response to questions 4, 5 and 6 of Section I above. Differences in national contract laws do not generally feature as a dominant obstacle to cross-border provision of insurance in practice.
4.	It is likely that B2C contracts (and possibly B2B contracts involving mass contracts) may be more affected by national contract laws.
5.	Please refer to the response to question 4 above. It is likely that mandatory contract law provisions impact B2C contracts (and to some extent B2B contracts involving mass risks) as there are likely to be more such provisions applicable to mass risks than large risks.
6.	It is not possible to give an indication of the types of insurance most affected.

7.	It is likely that the national contract law provisions listed in section II of Discussion Paper II impact, to varying degrees and in accumulation, the provision of cross-border insurance. In practice, however, differences in national contract laws remain a minor aspect of the totality of obstacles considered and weighed up when insurers consider offering insurance cross-border within the internal market. By way of example, one of our members quantifies contract law issues as making up only 10% of all obstacles so considered and impacting the decision to supply cross-border insurance.