The Future of the Insurance Block Exemption Regulation – or How Special is the Insurance Sector?

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Subject to certain conditions, the current Insurance Block Exemption Regulation (BER)\(^1\) exempts important forms of cooperation in the insurance industry from the application of the prohibition of anti-competitive practices in Article 81 EC Treaty, namely:

- joint calculations, tables and studies,\(^2\)
- standard policy conditions (SPC),
- pools and
- security devices\(^3\).

The BER will expire by default on 31 March 2010. Under the Implementing Regulation\(^4\), the European Commission is required six years after its entry into force, to submit a report to the European Parliament and Council on the functioning of the BER together with any proposals for amendment in the light of experience.

The Commission started its review of the functioning of the BER in April 2008, launching a consultation.\(^5\) In addition to the consultation, the Commission sent questionnaires to certain stakeholders, public authorities and consumer organizations. Also, the national competition authorities have been closely involved in the review.

The consultation was centred on the following questions:

- Do the business risks or other issues in the insurance sector make it special and different to other sectors?
- Does this lead to an enhanced need for cooperation?
- If so, does this enhanced need for cooperation require a legal instrument like the BER to protect or facilitate it?
- If so, is the current BER the most appropriate legal instrument?

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\(^2\) In the following the term “joint calculations” also includes tables and studies.

\(^3\) The term “security devices” is used in this article to include all technical specifications, rules or codes of practice exempted in Article 1 lit. f BER.


The findings of this review as well as the preliminary views of the Commission on the future of the BER are outlined in its Report to the European Parliament as well as the accompanying Working Document which were published in March 2009.

On 2 June 2009, the Commission held a public event in order to hear further comments on the Report and the Working Document. Separate panels discussed each of the four categories of agreements currently exempted by the BER. Following the event, the Commission sent around additional questionnaires seeking proof for the arguments that were put forward at the public event.

The present article summarizes the Commission’s preliminary findings on the functioning of the BER in the Report and the Working Document as well as the state of discussion during the public event. Furthermore, it analyses the approach taken by the Commission in the Report as well as the possible consequences for the insurance industry in Europe.

A. Preliminary Findings of the Report and Public Event

I. Joint Calculations

Subject to certain conditions, the BER exempts agreements which relate to the joint establishment and distribution of:

- calculations of the average cost of covering a specified risk in the past,
- calculations in connection with insurance involving an element of capitalization, mortality tables, and tables showing the frequency of illness, accident and invalidity (tables);
- the joint carrying out of studies on the probable impact of general circumstances external to the interested undertakings, either on the frequency or scale of future claims for a given risk or risk category or on the profitability of different types of investment and the distribution of the results of such studies.

In principle, the Commission is inclined to renew the exemption for joint calculations. Following the logic of the key questions outlined above, the major arguments are as follows:

- The insurance industry is indeed special and different to other sectors in the sense that the costs of an insurance product are unknown at the time the price is agreed and the risk covered. This fact leads to an enhanced need for cooperation because access to past statistical data is crucial to technically price the risk.
- Even the slightest risk that expiration of the BER will lead to less pro-competitive cooperation in this field shall be avoided. In particular large insurers may lack an incentive to (continue to) share their data with small and medium sized insurers or new market entrants if the condition to make the joint calculations available on reasonable and non-discriminatory terms, which is currently a requirement for exemption in the BER, no longer applies.

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Nevertheless, coming to the question of the appropriate legal instrument, the Commission expresses some reservation as to renewing the exemption in its entirety. Instead, the Commission contemplates to:

- narrow the scope of the exemption on the basis of risk type, namely to limit it to low frequency risks;
- add a transparency requirement such that shared information should be more easily/freely accessible to non-insurance companies such as consumer organizations or private individuals.

During the public event, further proof of the alleged need for and positive competitive effects of joint calculations was requested before the intended renewal of the BER in this area would be finally decided. The Commission answered that request by sending around additional questionnaires in the aftermath of the public event.

II. SPC

Subject to certain conditions, the BER currently exempts the joint establishment and distribution of non-binding SPC for direct insurance and non-binding models on profits.

Based on the following findings, the Commission does not intend to renew this exemption:

- SPC are not specific to the insurance sector, thus no sector specific exemption is justified.
- No legal instrument is necessary to facilitate cooperation on SPC:
  1. Most SPC are unlikely to fall within the prohibition of Article 81 (1) EC Treaty.
  2. If they do, it is unlikely that they would fail to comply with Article 81 (3) EC Treaty if they were in line with the requirements set out by the current BER.
- SPC may give rise to competition concerns due to the negative effects they may have on product differentiation and the lack of customer involvement in the drafting process. Such effects can only be adequately assessed in the context of a specific product and geographic market, meaning in the framework of an individual assessment under Article 81 (3) EC Treaty.
- There is no real risk of less or no cooperation in the event of non-renewal of the BER.

At the public event, some of the panel members supported the Commission’s view that there is no need and/or no justification for a renewal of the BER in this area. From a consumer perspective concerns were voiced that the joint establishment of SPC leads to unfair clauses.

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8 Panel Member from FIN-USE, Forum of User Experts in the Area of Financial Services.
9 Panel Member from Test-Achats, Belgium.
III. Pools

The BER exempts the setting-up and operation of insurance pools for the common coverage of new risks for three years from the date of first establishment of the pool, regardless of the market share of the pool.

Regardless of the novelty of the risk and subject to certain conditions, in particular market share thresholds, the BER furthermore exempts co-insurance or co-reinsurance pools that provide common coverage of a specific category of risks.

In the Report, the Commission expressed its intention to renew the exemption of pools based on the following findings:

- Risk sharing for certain types of risks (e.g. very large risks or new risks) is crucial in order to ensure that these risks are covered.
- This aspect is specific to the insurance sector and requires enhanced cooperation.
- There is some risk of non-cooperation in the event of non-renewal. Even if not significant, it may be appropriate to keep an exemption at least for some time.

While supporting a renewal of the exemption for pools, the Commission made it very clear that the current text of the BER will be significantly changed. In particular, the Commission intends to return to its former method of market share calculation which took into account the pool members’ global turnover in the relevant insurance market, irrespective of whether they do their business through the pool or independently.\(^{10}\) It believes that the current method of calculating the market share which only takes into account the insurance products underwritten in the pool is not in line with other rules on assessing forms of horizontal cooperation and thus constitutes an unjustified preferential treatment of the insurance sector. There are no indications in the Report if and how the market share thresholds will be changed in the future BER.

At the public event, Commissioner Kroes additionally pointed out that the Commission thinks that there are “some alarming practices concerning pools. In particular: the way many insurers are neglecting to carry out the careful legal assessments of their activities required by the Regulation” and added that the Commission will keep “a close eye on the industry, using strong enforcement where needed”.\(^{11}\)

At the public event, the majority of the panel on pools agreed that pools were vital to generate capacity or know-how in certain situations. However, views varied widely to what extent market share thresholds should be a condition for exemption and if and how the need for pooling certain risks should be continuously (re-)assessed over time.

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IV. Security Devices

Subject to certain conditions, in particular the lack of harmonized EU standards, the BER currently exempts agreements with respect to the establishment, recognition and distribution of:

- technical specifications, rules or codes of practice concerning security devices and procedures for assessing and approving the compliance of security devices with such specifications, rules or codes of practice;
- technical specifications, rules or codes of practice for the installation and maintenance of security devices and procedures for assessing and approving the compliance of undertakings which install or maintain security devices with such specifications, rules or codes of practice.

Based on the following findings, the Commission does not intend to renew the exemption for security devices:

- Standard setting procedures are not unique to the insurance sector.
- Setting standards for security devices on a national level may present obstacles to the cross-border marketing of security devices (free movement of goods and services).
- Even if the insurers are legally free to insure property protected by non-compliant devices, the standards often become de facto mandatory. This may lead to a lessening of competition on the downstream market for security devices.
- Involvement of all interested parties as well as access for third parties on fair, reasonable and non-discriminatory terms are considered important requirements for an individual exemption of a standard setting procedure under Article 81 (3) EC Treaty. The BER, however, does not adequately reflect these requirements.

To be able to assess whether the positive effects of standard setting for security devices on risk prevention and insurability, which are generally recognized, outweigh the potential negative effects of market partitioning and foreclosure identified in the Report, the Commission advocates a case-by-case analysis under Article 81 (3) EC Treaty based on some form of guidance from the Commission, potentially in the framework of the Horizontal Guidelines which are currently also under review.

The panel on security devices at the public event was split on the Commission’s findings. One panel member confirmed this assessment by referring to alleged negative effects of multiple national testing and certification for marketing innovative products throughout the EU. Another panel member stressed the precedence of European standard setting in the framework of CEN and CENELEC over joint standard setting by the insurance industry which lacked transparency. The panel members from the insurance industry disagreed and stressed the positive effects of national standard setting (see Sec. B.IV.).

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13 Panel member from Euralarm, an association of European manufacturers and installers of fire and security systems.
14 Panel member from DG Enterprise, European Commission.
B. Analysis of the Preliminary Findings

I. Joint Calculations

1. Renewal of the BER

The Commission’s intention to renew the BER for joint calculations is to be welcomed. It is supported by the numerous submissions of interested parties in the course of the consultation and a broad consensus between the members of the expert panel at the public event.

As pointed out in the Report, insurance is a legal product which covers future risks, the realization of which is – by nature – unknown at the time the contract is concluded. Consequently and different from other industries, the costs of the individual product are unknown at the time the price is agreed. To address this special feature of insurance, joint calculations are fundamental for a rational calculation of premiums and provide all companies concerned with the same competitive starting point.

In that context, the overriding principle is the law of large numbers according to which statistical projections become more accurate the more risk data is available. Given the limited data base available to smaller and medium-sized companies as well as new market entrants, these market players depend upon the availability of joint calculations to be able to assess the risks with a sufficient degree of accuracy. However, even large companies do not have sufficient information available in all of the segments so as to be able to derive statistically valid data. In addition, the loss situation in an individual company can differ completely from that of the (overall) market, so that access to joint calculations is required for validation purposes. Without relevant valid joint calculations insurers would have to apply higher risk and venture premiums in certain segments or even refrain from underwriting certain risks altogether. Finally and contrary to the clear intention of the BER to promote statistics with as much detail and differentiation as actuarially adequate, the possibility for premium differentiation would be reduced.

The current BER expressly recognizes these facts and concludes that joint calculations promote competition by helping smaller insurers and facilitating market entry, thus benefiting consumers. No doubt, this assessment is absolutely valid until today and justifies a continuous block exemption.

In addition, complying with future solvency capital requirements will require the use of high quality statistical data to provide for efficient capital allocation in the interest of policyholders and beneficiaries. Therefore, it seems counter-productive to limit the possibilities for collecting such data under the safeguards of the BER just when implementation of the Solvency II directive approaches.

2. Limitation of the Scope of Exemption

Joint calculations should only be exempted by the BER to the extent that they are necessary to produce the efficiencies outlined above. Therefore, it is perfectly legitimate for the Commission to pose the question whether the scope of the exemption should be limited. The answer to that question is no.
In particular, a limitation to low frequency risks under the assumption that the insurers should have a sufficient data base for the calculation of high frequency risks is not justified, as the following arguments show:

- The need for access to a large data base equally arises in the case of low as well as of high frequency risks.
- For a reliable calculation of a risk, it is the number of claims per category and not the overall claims frequency that is decisive.
- Major single losses may lead to significant calculation insecurities even for high frequency risks. In case of a limited database, major losses may even multiply claims expenditure.
- High and low frequency components may be combined in one insurance product. Therefore a limitation of the exemption to low frequency risks would create significant problems of definition and differentiation in particular as such definition would have to be equally suitable for different types of insurances and the insurance industry throughout the EU. At the same time one would have to ascertain that such differentiation would not negatively affect the usefulness of the statistics which continue to be exempted.

Therefore, it is neither advisable nor justified to limit the scope of the exemption of joint calculations to low frequency risks. The exemption should be renewed as is.

3. Additional Transparency Requirements

The BER already demands that the results of the joint calculations be made available on reasonable and non-discriminatory terms to any insurance company that requests a copy of it. This requirement is necessary but also sufficient to ensure an appropriate level of transparency. Additional transparency requirements e.g. free access of non-insurance companies seems to be counter-productive and could pose a real threat to the continuous cooperation in this field.

Free access for third parties would de facto mean that any insurance company would be able to obtain the information of interest to it without having to put in the significant effort of providing relevant data itself. As a consequence, companies might in future refrain from providing the necessary information threatening the actuality and validity of the calculations.

Such a risk should only be undertaken if the aim pursued with free access for third parties is tantamount. To assess if that is truly the case one would first need to determine what concerns are to be addressed and whether free access is the best remedy. At this stage, it remains unclear what is to be gained from free access e.g. for consumers. The data is meant for actuaries and controllers and is quite complex. It is therefore not perceivable what informational value can be drawn from it without expert knowledge.
II. SPC

The Commission’s competitive assessment that SPC generate positive effects (e.g. comparability of products) and generally do either not impede competition or are at least exempt under Article 81 (3) EC Treaty is convincing. However, that assessment in itself does not justify a refusal to renew the BER in this respect. On the contrary, it even forms the basis for a block exemption regulation.\(^{15}\)

As concerns the specificity of SPC to the insurance sector, it is true that standard business conditions are also common in other sectors. However, given the fact that insurance products are legal products, the insurance cover is originally embodied in the policy conditions, which give rise to the insurers' performance obligation in the first place. This fact significantly increases the need for legal certainty as to the contents of these obligations, which is to a large extent provided through SPC. Furthermore, there is a link between SPC and the statistical work in the insurance sector. SPC support joint calculations because they ensure a joint fundamental understanding and, thus, a comparable data basis.

A similar situation cannot be found in other sectors which may be why representatives of the banking sector have argued that they do not require a legislative framework, which, however, can hardly serve as an argument against renewing the BER in the insurance sector.

Furthermore (at least) the Report and Working Document do not reveal any serious competition concerns that could not be resolved in the framework of a future BER e.g. by imposing (additional) conditions for exemption or providing possibilities for withdrawal. The concerns expressed with respect to product differentiation and customer involvement have been voiced only in very general terms without providing evidence or proving relevance beyond distinct cases which cannot be generalized.

Will cooperation in relation to SPC cease when the BER expires? Probably not. However, there is a risk of reduced cooperation as the companies will have to bear a greater risk of legal uncertainty which will need to be addressed in the context of individual self-assessment which the Commission rightly emphasizes will “need to be undertaken in the context of the product and geographic market” for which the SPC are intended. Such self-assessment will be more time consuming and costly than assessing compliance with the requirements of the current BER. The issuance of guidance may attenuate but not cure this effect as it will not be legally binding upon the national competition authorities and courts. Therefore, the question is whether taking that risk is justified in lack of convincing evidence of serious competition concerns which can only be addressed outside the framework of a BER.

Finally, a word of caution must be voiced against extensive requirements for consumer involvement in the process of drafting SPC. SPC must already be made available to any interested person under the current BER, so that the necessary transparency is ensured. Any obligation to regularly involve third parties, such as consumer protection organizations, in the drafting of SPC must be carefully weighed in view of the significant bureaucratic burdens and administrative expenses involved on the one hand and the

positive competitive effects to be achieved on the other. In this context it should be noted that SPC often are subject to legal requirements which ensure adequate protection of the policyholders’ rights (e.g. in Germany the German Insurance Policy Act and the provisions of the Civil Code on general terms and conditions). These provisions are best placed to achieve adequate consumer protection, not competition law whose aim is protecting the freedom of competition.

III. Pools

The Commission’s intention to renew the BER for pools is to be supported.

The Commission rightly points out that the necessary cooperation in institutionalized co-(re-)insurance pools will continue to require support in the form of sector-specific provisions laid down in the BER because pools give rise to positive effects such as an increase in the availability of capacity and the possibility for smaller and medium-sized insurers to enter or remain in the market.

The fact that some pools may currently not benefit from the exemption because they either do not even restrict competition because no individual insurer is capable of insuring the risks alone (e.g. nuclear or terror pools) or some pools may wrongly consider themselves covered by the BER does not change the validity of that assessment. Also, the fact that market definition is key and the BER cannot offer legal certainty in this regard does not serve as an argument against renewal: Undertakings are required to define relevant markets as part of their self-assessment under Article 81 (3) EC Treaty and the fact that they may err in this assessment does not rule out exemption as such.

Thus, it comes down to the question whether the current exemption needs redrafting with a view to market share calculation. The answer is no.

Contrary to the view held by the Commission, the method of market share calculation in the current BER does not constitute an unjustified preferential treatment of the insurance sector. Instead, the Commission rightfully amended the BER in 2003 to only look at the business generated by the pool when assessing compliance with the market share thresholds, because the market share of the pool alone is the correct basis for an assessment of its effects on competition. All communication between pool members especially with regard to quotas, premiums and conditions, solely relates to their joint risk sharing within the pool. To limit the competitive effects of a pool, the BER itself makes it a condition precedent to exemption that the competitive behaviour of the members outside the pool shall not be affected by the cooperation within the pool.

Against this background, taking into account the overall market share of the members of a pool would only be appropriate if it had to be assumed that membership in a pool, regardless of scope and size of the pool’s business, generally affects the competitive behaviour of the members outside the pool. This, however, does not correspond to economic reality.

Economic reality shows that the smaller the share of the business brought in a pool compared to the relevant pool members’ overall activity in the relevant market, the less

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16 The mentioned Aviation case (para 95 of the Working Document) is not representative of the insurance industry’s regular work on SPC in particular in the retail business.
17 See Article 8 BER.
plausible it is to argue that the members' behaviour is influenced by the cooperation in the pool. Obviously, an insurer rather takes 100% of a good risk than just a share. In these cases, the pool simply is an additional market player in a competitive market, often driven by the interests of intermediaries to develop products for certain customer groups.

On the other hand, if the share of the relevant business brought in a pool is high in comparison to the members' overall activities in the relevant market, the market share of the pool already reflects the competitive importance of the cooperation because in that case it approximates the overall market share of the members involved. Depending on the strength of the insurers involved, the market share thresholds of the pool would be exceeded either way and the envisaged change in the method of market share calculation proves unnecessary.

It is this limitation of competitive effects to the business of the pool that differentiates the competitive assessment of pools from other forms of horizontal cooperation, such as specialization or research & development agreements: The latter forms of cooperation are not limited to a clearly defined area to which specific market shares can be allocated by way of special business activities. Rather, these activities have a comprehensive influence on the overall competitive behaviour of the cooperating undertakings in the relevant market.

This shows that reference to the pool’s market share as a basis for assessing whether exemption is granted is not a preferential treatment of the insurance sector, but a differentiation that is appropriate in factual terms.

The market share thresholds are currently in line with thresholds for other forms of horizontal cooperation. Any reduction would put the benefits at risk that pools offer to their members, e.g. gaining the necessary experience of the sector of insurance involved or achieving reductions of premiums through joint reinsurance on advantageous terms.18

To the extent that the Commission expresses concerns that the current method of market share calculation might not deliver good results for particular market structures (e.g. oligopolistic markets), these concerns can and should be addressed appropriately on the basis of their exceptional character in the context of a withdrawal of the exemption.

Whether the Commission will keep or change the method for market share calculation, the ban on multiple pool memberships (Article 8 lit. f BER) should be deleted. First, the provision is impracticable for the undertakings involved. Second it does not afford a sensible competitive assessment of alleged group effects. Third, deliberate circumvention of market share thresholds by way of establishing or joining various pools in the same relevant market can be appropriately prevented by withdrawing the exemption. Additionally, in case the Commission should decide to return to the former method of overall market share calculation, a parallel ban on multiple memberships would no longer be consequential, in particular in view of the legislative history of this provision.

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18 See para 21 of the recitals of the BER.
IV. Security Devices

Cooperation on security devices in the insurance industry is hardly comparable to standardization procedures in other sectors which form the basis for the provisions on standard setting in the current Horizontal Guidelines.\(^{19}\) The latter focus on standardization procedures which are mainly driven by the production side in the interest of interoperability of products. In the insurance industry, cooperation on security devices is driven by undertakings which are neither producers nor sellers of the products/services to which the standards apply answering the need to prevent or minimize risk in the interest of the insured.

Nevertheless, cooperation on security devices may affect the markets for these devices. That is why Article 9 BER already imposes requirements on transparency of the standard setting process and on the non-discriminatory access to all standards. To the extent that the Commission believes that adequate involvement of the producer side should be a requirement for exemption, such requirement does not warrant a change of legal instrument as it could easily be introduced to the new BER. Its fulfilment is already market reality in many areas of the cooperation on security devices, today.

Also the aspect of free movement of goods/services is already reflected in the BER: No exemption where there exist at Community level technical specifications, classification systems, rules, procedures or codes of practice harmonized in line with Community legislation (Article 1 lit. f BER). Any form of cooperation which does not respect these limits clearly is outside the scope of the BER, already today. In addition, Article 6 lit. k BER denies exemption to SPC which exclude or limit the cover of a risk if the policyholder uses security devices, or installing or maintenance undertakings, which are not approved in accordance with the relevant specifications agreed by associations of insurers in other member states or at the EU level.

Obviously, EU-harmonized standards can better serve the Common Market. However, one should duly consider that (i) standardization at national level often is the starting point for harmonization at EU level; (ii) there are still national differences in risk situations which cannot be dealt with at a harmonized level, (iii) there are areas with only very few or no EU-harmonized standards (e.g. for the installation and maintenance of security devices).

Against this background and based on the fact that only very limited input was received from the producer side during consultation, it seems that the competition issues arising in the context of the cooperation on security devices are or at least can be adequately dealt with in the framework of the future BER. Given the importance of this form of cooperation for effective risk prevention through the EU benefiting all consumers, it seems questionable whether non-renewal of the BER in exchange for some form of informal guidance is efficient and pro-competitive. In any case, such guidance would have to pay tribute to the specificities of standard setting in the context of security devices. If such guidance is to be given in the framework of the Horizontal Guidelines, significant changes will be required to the current text.

\(^{19}\) Para 159 et sqq, fn 12.
C. The Way Forward

The Commission will now analyze the comments received since the publication of its Report and in response to its additional questionnaires and decide whether to renew the BER in whole or in part. It is expected that the general course of action as concerns the areas for renewal and non-renewal will not change. But the details of the scope of the future BER and the form and scope of guidance for the parts that will not be renewed are still open.

For the parts of the BER that will be renewed, the Commission will start the internal drafting process. In autumn of this year, the Commission will then publish a draft regulation for public consultation. In addition, a publication will be issued with respect to the parts of the BER that will not be renewed. Possibly, some of these parts, most likely the cooperation on security devices, will be dealt with in the revised Horizontal Guidelines. All changes to the current BER will require adaptation of business processes and should therefore be accompanied by an adequate transitional period.

And the insurance industry? Will it continue to operate based on a limited BER? Of course! Will it operate as efficiently as before? One would hope so! Whether that hope will materialize will depend upon the substance of the future set of rules. Participation in the process of drafting these rules is therefore key for the insurance industry.

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Allianz SE is the parent company of the Allianz Group, one of the leading integrated financial services providers worldwide. With nearly 155,000 employees worldwide, the Allianz Group serves approximately 75 million customers in about 70 countries. On the insurance side, Allianz is the market leader in the German market and has a strong international presence. In fiscal 2008 the Allianz Group achieved total revenues of over 92.5 billion euros. Allianz is also one of the world's largest asset managers, with third-party assets of 703 billion euros under management at year end 2008.

In 2006 Allianz SE became the first company in the Dow Jones EURO STOXX 50 Index to adopt the legal form of a Societas Europaea, which is a new European legal form for stock corporations. Allianz SE shares are traded on all German stock exchanges as well as in London, Zurich, Paris and Milan. Moreover Allianz became the first German financial services provider to have its shares listed on the New York Stock Exchange, where they have been trading in the form of American Depositary Receipts (ADR). 100 percent of the stock is free float.