Position Paper

# EICL - Response to Discussion Paper V

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| Our reference: | SMC-LEG-13-084 | Date: | 24 September 2013 |
| Referring to: | Discussion Paper V | | EC expert group on European insurance contract law |
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| Pages: | 9 | Transparency Register ID | 33213703459-54 |


## Summary

Insurance Europe welcomes the opportunity to comment in writing on Discussion Paper V, forming the basis of discussions during the fifth meeting of the expert group on European insurance contract law (EICL) (held on 9-10 September 2013), and the relevant section of the final report that will represent the work-output of the expert group by the end of 2013.

Insurance Europe continues to be supportive of the objective of the work of the expert group. It has previously noted its concerns over the organisation of the expert group and the procedural rules applying to the expert group. Following discussions between Insurance Europe and the Commission at the last meeting of the expert group, potentially detrimental procedural rules may now be applied to the expert group and its work. Insurance Europe raises these genuine concerns in the spirit of collaboration and a desire for active participation in the work of the expert group. Insurance Europe would very much appreciate if the Commission would consider the impact some procedural rules may have on the quality and credibility of the final report of the expert group, the purpose of which is to advise the Commission on the mandated question.


## Overarching comments

### Procedures

Insurance Europe's members wish to participate as actively and constructively in the work of the expert group as possible. To this end, Insurance Europe believes that procedural rules should allow members of the expert group, including representative organisations, to provide constructive substantive input to the work of the expert group. This is currently difficult to do due to the tight timeframes being set for comments and if written comments after meetings are no longer permitted. Insurance Europe is also of the view that important discussions within the expert group, such as on the extent of the mandate of its work, should be permitted within the procedural rules and that the weight of contributions which representative members, such as Insurance Europe, make are safeguarded.


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In the spirit of collaboration and reflecting Insurance Europe's members' desire to contribute actively and constructively, Insurance Europe would ask the Commission to reconsider the volume of materials necessary for reflection and input in what are very tight timeframes, and the impact which *ad hoc* procedural rules may have on the quality and representativeness of the final report.

## Organisation

Insurance Europe wishes to contribute as much and as constructively as possible to the work of the expert group. The organisation of the work of the expert group should however enable members of the expert group to do so, to **avoid jeopardising the outcome of the work of the expert group**. In particular, there is a real risk that the input the European Commission seeks, and the timeframes permitted to collate and develop responses, jeopardise the ability of the European insurance industry, through Insurance Europe, to be as constructive as is desired by the industry.

## Scope of work

Insurance Europe is **concerned to see that several issues raised in the discussion papers are not matters of contract law but rather reflect differences in national regimes, legal, regulatory and taxation regimes, diverse national general best practice rules and cultural practices that are specific to each jurisdiction.** Insurance Europe has in previous responses to Discussion Papers noted that aspects raised were not within the mandate of the expert group as they did not amount to contract law issues. During the last meeting of the expert group on 9-10 September, the issue of the scope of the work of the expert group arose – in the context of liability insurance for lawyers – with a wider implication for the work of the expert group. Insurance Europe would ask the Commission to launch further discussions of the scope of the work of the expert group within the expert group in order to ensure that non-contract law issues are not mistakenly included in the scope of the work of the expert group. In particular, issues such as risk evaluation, pricing and product design are not contract law issues, but arise from, and must remain within, insurers' freedom to contract.

During the last meeting of the expert group, there was some discussion on whether reinsurers would benefit from a harmonised European insurance contract law, on the basis that underlying insurance contracts would then be subject to uniform triggers. **The need to leave reinsurance out of the scope of the work of this expert group is imperative to safeguard the continued capacity that reinsurers offer insurers.** The reinsurance market has historically been permitted substantial freedom to contract in a bid to safeguard the availability of sufficient reinsurance capacity to support the insurance markets. It is imperative that this remains so, as any unforeseen consequences on the reinsurance markets could seriously jeopardise the insurance markets to the detriment of consumers.

## Lack of evidence

Thirdly, **it remains unclear whether there is any evidence to suggest that a cross-border insurance market would develop** if differences in contract law were removed. No evidence has been provided to suggest that there would be any demand for these products that would warrant the resulting business costs associated with the supply of cross-border insurance products. Further, no evidence has been presented to show that consumers, businesses or insurers would benefit substantially from any attempt to address differences in national contract law provisions.

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, language, culture (including expectations of the local policyholder), the form and prevalence of frauds, the legal, regulatory, supervisory and taxation environments.

Likewise, there is no certainty that consumers would willingly take up cross-border products. 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 V, Section | Insurance Europe response |
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| **1.** | **Economic impact** |
| | While the discussion paper states that the liability insurance market represents only 7% of the non-life insurance premiums of European insurers, Insurance Europe questions the source of this figure and disputes its accuracy. For instance, Insurance Europe's August 2013 "Key Facts" brochure, which illustrates the statistical composition of the European-wide insurance market pursuant to feedback received from its members, provides that general liability insurance premiums account for 11% of the European-wide Property & Casualty insurance market (i.e. non-life insurance). In this respect the liability insurance market would appear to be larger than the figure mentioned in the discussion paper.<br><br>The discussion paper also fails to note that some liability markets are more developed than others and for this reason may take a more prominent position in a member state's individual non-life insurance market. The size of a liability insurance market highly depends on the history of market development, the competitiveness of the market and the effectiveness of a member state's liability regime (in other words, a higher number of liability claims leads to higher demand for applicable liability insurance products).<br><br>For example, liability products account for 13% of general liability insurance premiums in the UK and is thus considered to be one of the main sectors of the UK non-life insurance market. The UK, alongside other member states such as France and Germany, is more likely to have a larger liability insurance market than those member states where insurers have less experience with managing and handling liability claims, such as is the case with many countries in Eastern Europe. The liability insurance markets in Eastern Europe are still developing in order to accommodate new waves of liability legislation; however, they may have not reached the levels of a larger market that has dealt with liability laws for a significantly longer period of time. This also contributes to different sectorial premium percentages for individual markets. |
| **2.** | **Compulsory nature** |
| | While member states may introduce their own forms of compulsory liability insurance for cultural, economic or political reasons, EU-wide compulsory liability insurance proposals would not provide "one size fits all" solutions; as the likelihood of their success depends on the characteristics of the liability to be covered as well as the capacity and expertise of the respective liability insurance market. The Dutch legislator, for example, deems it generally not necessary to lay down laws for compulsory liability insurance for consumers (except of course in motor liability insurance) and households, although in many areas liability insurance is compulsory for professionals or necessary to become a member of an organisation of professionals.<br><br>The pure existence of differences in risk suggests that member states may consider different compulsory insurance laws for various sectors (if they mandate insurance at all). Diverging liability laws, legal practices, different approaches towards risk management between member states, and differences in compulsory insurance measures are not, in fact, contract law issues, but rather inherent member state differences that impact and influence insurance product design. While national compulsory insurance laws may differ, this is, as explained above, a logical consequence of the diverse national liability regimes rather than as a result of contract law.<br><br>However, the challenges in offering a cross-border product that is in line with national laws and culture is not unique to the insurance industry. There are sector-specific issues that any company must evaluate and resolve prior to conducting business in another member state, including: |

- language barriers;
- different licensing, legal regulatory and taxation systems;
- diverse national general best practice rules;
- cultural practices that are specific to each jurisdiction;
- whether a physical presence in the member state is required; and
- the availability of data for the respective market.

Additional non-contractual factors that insurers must particularly consider include:

- the level of experience and familiarity with national liability laws in the other member state;
- additional resources for the handling and managing of claims filed in the other member state;
- the level of demand for the cross-border cover is low and is likely to be a result of insured professionals themselves being organised in their cross-border offerings through local subsidiaries or networks of professionals; however, where there is a need for cross-border liability insurance, cover does exist;
- insurer capacity to cover potential claims while still fulfilling its other financial obligations (e.g. solvency requirements and financial obligations to investors); and
- the feasibility for an insurer to maintain a continuous and flexible relationship with policyholders domiciled in another member state (whether permanently or temporarily).

As a result of the above inter-related factors, the provision of a cross-border liability insurance product is not something that can be undertaken easily by all insurers. Insurers must be capable of offering products that reflect the comprehensive local market and risk analysis for the target member state. This analysis should cover all aspects of product design, including policy wordings, pricing (i.e. premiums), underwriting, risk management and claims handling processes, distribution and reinsurance. In most cases, this requires the development of an entirely new insurance product. The costs in conducting this analysis and subsequently adapting (or in some cases, creating) a liability insurance product could thus go well beyond the risk appetite and/or capability of an insurer. All these are factors that must be considered when deciding whether to offer insurance services cross-border.

Finally, a distinction should be made between liability products that are compulsory by law (e.g. motor and employers' liability insurance) and those liability products that are compulsory by regulators (e.g. professional indemnity insurance). In the latter case, the compulsory nature of products cannot be achieved solely through changes in the compulsory insurance law itself, which for the above-stated reasons would already be complex and extremely challenging

**3. Occurrence based v claims-made policies**

Regarding traditional liability insurance policies, insurers are not obliged to indemnify or defend "any loss which allegedly occurred" during the policy period. Before the applicability of insurance can even be considered, there must be a link made between the insured's actions and the loss, also known as "causation"; in other words, the insurer only becomes obliged to defend/indemnify when the actual injury or damage occurs and if causation is established. If this does not occur the nature of liability is not recognised, in which case the insured's liability insurance policy would not be applicable. Thus, it is incorrect to imply that the mere existence of an insurance policy guarantees compensation to an injured party.

In addition to the above, the liability of an insured may be negated by a supervening event (e.g. negligence caused by a third party outside the claimant and the insured) or when the loss which arose from the insured's activities is deemed unforeseeable (e.g. in cases of crime or fraud or force majeure). Additionally, any contributory negligence on the part of the claimant could impact the applicability of cover, though this depends on whether a member state has contributory negligence laws and, if so, the criteria for this form of negligence.

In citing the occurrence of the event as the general trigger for insurance, the discussion paper neglects the increasing use of claims-made insurance policies in many of the newer member states as well as in the field of professional indemnity. Even the definition of "occurrence" varies widely across Europe, as it is highly dependent on the interpretation made by the insurance contracts as well as by the national courts.

Thus, the triggers and scope of insurance products vary across the member states for a variety of reasons. This variation in triggers across product types and markets has developed to accommodate differing circumstances.

For example, a defective product design leading to a personal injury claim can be covered by a product liability policy in some member states (as in the UK), while in other member states it might be covered by a professional indemnity policy or else not covered at all (e.g. in another member state where product liability insurance is not widespread).

There are moreover inaccuracies with respect to the representation of the UK market. On page 4 of the discussion paper it states that the UK adopted a claims-made approach following several tort cases, such as in the asbestos field. However, the main liability product in the UK – employers' liability insurance – has always been, and still is, sold on a causation basis, although the cause can be on-going for very long periods, leading to multiple policies being triggered.

The trigger of a policy, as for instance claims-made cover in the area of medical liability insurance in France, is a key element for insurers to control their exposure and is a fundamental condition of financial capacity to cover long-term risks. The trigger that applies to a policy is intimately linked to the risk insured as different risks lend themselves to different triggers.

For all these reasons, the final report should acknowledge that the triggers and scope of insurance products vary across the different product lines and across different member states.

**4. Extent of cover**

**4.1 Insured sums**

The amount of cover offered by insurers is largely based on the economics of the jurisdiction where the risk is located and, hence, the factors that lead to the expected cost of that risk (e.g. average medical costs associated with personal injury actions, amount of damages likely to be awarded in a national court, etc.). For instance, a 5M EUR liability claim in one country may be worth just 100K EUR in another, as awards tend to be greater in Western European countries than, say, Eastern European countries, due to cultural differences in the willingness to litigate and the economic reality of the market. In light of this, it would be very difficult for, for example, a Lithuanian-based insurer – that is experienced with Lithuanian-sized claims amounts – to adjust its financial capacity to accommodate, say, UK-sized litigation costs. The understanding is that this difference in the offering of insured sums stems from diverging economic situations rather than insurance contract laws.

**4.2 Cover for legal costs**

Liability insurance policies often cover these costs, however the decision and practice of doing so is up to the individual insurer. It is also worth noting that the possibility for an insurer to cover these costs is, yet again, entirely dependent on the costs associated with the local risk(s). Legal fees vary greatly between member states depending on the litigation culture and the demand for legal representation. For this reason, insurers will need to assess whether they can cover such fees in a cross-border case, particularly if they are significantly greater than the fees they currently cover in their home jurisdiction.

**4.3 Deductibles**

Deductibles are integral to maintaining an insurer's financial capacity, as they can help to limit the number of claims by allowing policyholders to handle more manageable, smaller claims by themselves. Deductibles also have the added benefit of incentivising policyholders to exercise

high risk management in order to avoid that their activities result in potential claims.

National legislations establishing maximum deductibles reflect political decisions to protect third parties suffering damages. Within this framework, policyholders and insurers can then exercise their freedom to contract in order to reach a negotiated deductible that suits both parties.

The discussion paper also claims that "*[i]n some countries there are mandatory minimum covers, but the insured amounts differ*". Insurance Europe suggests that competition, rather than contract law, is the main factor in a case where one insurer is willing to give a lower deductible (and hence a higher "insured amount") than another insurer (which may offer a higher deductible with a lower "insured amount"). Competition in this respect is often most beneficial for consumers, as the ability to negotiate on this point generally offers more choices between liability insurance products.

**5. Causation and mitigation of the loss**

In line with Insurance Europe's response to Section 3, it should be noted that the interpretation of causation and mitigation varies across the EU. A risk may be considered higher, for example, in a jurisdiction where causation is more widely established in national law than in another jurisdiction where causation standards are more difficult to prove. National laws also vary on whether either a liable party or the claimant has the responsibility to mitigate loss, regardless of the existence of a liability insurance policy. Triggers (as also discussed in Section 3) are based on liability legislation and the interpretation of national courts, which will inevitably depend on the facts surrounding each individual liability claim. Accordingly, whether insurers need to adapt their products due to causation or mitigation issues reflects wider local law rather than differences in insurance contract laws.

Rules on causation and mitigation of loss differ widely between member states. Under Dutch civil law, for example, there are extensive rules on causation laid down in the Civil Code and extended by case law. This illustrates that a knowledge of local civil laws in general is necessary.

It is also worth mentioning the example of the EU Products Liability Directive which requires a causal link between the defective product and the claimant's injury. However, it is up to the member states to identify the criteria for establishing that causal link when bringing a product liability claim, after which the national courts will be charged with the responsibility of interpreting whether such a causal link for a claim has been established. Therefore, alongside other factors to be considered, product liability insurers must also be mindful of how the member states have implemented the EU Product Liability Directive – and the costs that may be associated with the adopted national legislation – should they wish to offer cross-border cover.

**6. Direct claims of 3rd parties & assignment**

Provisions on direct actions against insurers are highly diverse in Europe. In some member states there is no right of direct action afforded to a third party (i.e. the claimant) or there may otherwise be strict legal criteria for establishing that an insurance policy is intended to benefit a third party. The UK, for example, has no common law right to file a direct action claim against the insurer and Germany similarly does not provide for third party rights against an insurer unless a compulsory insurance is affected and the policyholder is insolvent or his residence is unknown, §115 German VVG (with the exception of compulsory insurance for motor vehicles, which is regulated by the EU Codified Motor Directive). France, on the other hand, permits third parties to bring direct actions if they can demonstrate they have suffered damage due to the insured's actions.

As claimants are often only entitled to damages that are covered within the scope of the applicable insurance (i.e. the claimant stands in the shoes of the insured), it is further unlikely that insurers' costs would be significantly increased in other member states that allow direct

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| | actions, thereby deterring an insurer from entering those member state markets. However, Insurance Europe maintains that such "rights" are closely tied to national civil laws and thus do not represent insurance contract law issues. |
| **7.** | **Subrogation** |
| | Subrogation is a common practice within the insurance industry, particularly to ensure fairness and to prevent double recovery of costs/damages. The practice, however, varies between member states. In the UK, insurers are entitled to subrogation as a matter of common law, though such subrogation rights may be waived under contractual terms (as is the case with the offshore oil industry). In Germany, subrogation is available to the extent that the insurer indemnifies the insured, though the transfer of rights cannot be relied upon to the insured's detriment. In France, the insurer may be automatically subrogated to the insured's rights against a third party causing the damage (e.g. a supervening cause) after paying the insurance indemnity. Statutory subrogation in France applies where payment of the indemnity was legally due under the insurance contract.<br>The above examples are closely tied to the national laws covering civil actions and the legal right to recourse against another party.<br>Coverage is partly offered by insurers on the basis of their knowledge that subrogation is a possibility, thus there may be financial risks when offering coverage without specific knowledge or understanding of the possibilities for subrogation. Furthermore, mandatory laws and case law should be assessed before offering coverage in another member state because the options for subrogation may be very different from the insurer's home member state.<br>In addition, Insurance Europe agrees with the acknowledgement within the discussion paper that there is no evidence that subrogation poses a specific problem for insurers seeking to offer cover in another jurisdiction. As subrogation does not pose any detriments to consumers and as this is not linked to contract law issues, it remains unclear why this is considered in discussion paper V. |
| **8.** | **Liability insurance for lawyers** |
| | It is stated in this section that liability insurance for lawyers "provides a necessary guarantee for the clients in case of an error or fault committed by the lawyers". As discussed in Section 3 ("Occurrence Based versus Claims-Made Triggers"), this statement is inaccurate. Insurance policies are designed to protect the insured party (i.e. the lawyer) from potential claims. Depending on the individual facts of a claim, in conjunction with the policy's terms and conditions, professional indemnity insurance for lawyers does not *guarantee* compensation to their clients.<br>As each member state operates under different legal and regulatory regimes, including the influence on professional certification by the different Bar associations, the requirements for obtaining liability insurance as a lawyer can differ across the EU. In Greece, Italy and Latvia, for example, this type of insurance is voluntary, while it remains compulsory in other member states. The means of obtaining this insurance from the market also differs; for example, in Germany a lawyer must personally obtain his or her professional indemnity insurance while the Bar in Belgium offers a collective insurance to all its members (the premium being reflected in their Bar registration fees) and in France it is through the local bar that such insurance is obtained. This could reveal, for example, that policy wordings in Germany vary more widely than the policy wordings in Belgium.<br>Considering the above, professional indemnity insurance for lawyers is closely tied to the member state's legal regime for the practice of law within its jurisdiction, including those requirements set forth by the state Bar. These are not related to insurance contract law issues, but are a reflection of differences amongst national professional bodies and the various national legislative, regulatory and taxation issues associated with the legal profession.<br>With respect to the territorial scope of cover, an insurer must make a decision whether to |

extend existing cover to another jurisdiction in light of:

- the various Bar requirements;
- the policyholder's experience with the foreign jurisdiction;
- the insurer's own familiarity with the liability laws pertaining to the legal profession;
- legal malpractice costs associated with the foreign jurisdiction; and
- the differences in culture and language.

All these factors contribute toward a higher risk of covering the policyholder in the foreign jurisdiction, thus often raising the cost of insuring that risk considerably. In some cases, an insurer is unable to assume these higher costs and may decline to extend cover, but this is an individual business decision based on their risk evaluation rather than deriving from insurance contract law issues.

In the experience of some of Insurance Europe's members, lawyers aiming for a multi-national practice tend to establish offices with local lawyers of other member states or otherwise enter into international co-operations with local law firms to ensure the quality of their services. In this case, the local officer or co-operation partner can and will take out a local insurance policy that is tailored to the member state's risk and legal environment.

**9. Liability insurance in the construction sector**

As in the response to Section 8 ("Liability insurance for lawyers"), the decision to offer construction liability insurance cross-border is foremost a commercial decision based on the individual insurer's risk appetite reflecting the liability legislation, its expertise and risk management practices of the other member state. The particularities of diverse national liability laws for construction and the legal requirements relating to compulsory insurance (which are in themselves based on these liability laws) present a wide variety of insurance needs for the construction sector.

These above issues have, in fact, been reviewed in the Commission's project on European Organisation and Liability Insurance Schemes (ELIOS), which has run for several years pursuant to the launch of the EU Lead Market Initiative in 2007, the objective being to facilitate insurance to small and medium construction enterprises across Europe. The first stage of the project was completed with a final report dated 30 April 2010, in which it was concluded that harmonisation of the construction liability and insurance schemes would not be feasible. Now in its second stage, ELIOS 2 (also known as "the ELIOS Forum") aims to collect information on the criteria used by insurers in order to create a database at European level that would share information on construction quality/compliance brands, the risks inherent to construction and the different member state insurance schemes.

As noted in the ELIOS 1 final report (published in the Official Journal of the European Union, Contract No: SI2.ACPROCE021941000), the Commission examined the possibility of harmonising rules on constructors' liabilities and financial guarantees with the possibility of introducing a directive (p 112). However, the EC consultancy for this study concluded that attempting a "unified" system for the entirety of the EU "*neglects local specificities linked to technologies used, quality control, customs, building standards, climatic and geographic constraints, etc., leading to confusion and a possible reduction in the building sector's efficiency and quality*" (p 113).

The ELIOS 1 study evaluated the feasibility of a "European insurance contract" for the construction sector, but in the April 2010 final report it was advised that such a contract could not be implemented at this stage, as difficulties were presented by the "*diversity of liability systems of the Member States and of their building regulations*". The report noted that "*insurance schemes are developed within a wider context related in particular to administrative rules, construction requirements, the respective roles and responsibilities of each party involved, the quality signs and labels, the methods of risk assessment and prevention*" (p 117).

As illustrated in the above portions of the ELIOS April 2010 report, there appears to be no

evidence that the difficulties associated with performing cross-border construction in light of insurance obligations do not result from diverging insurance contract laws. Rather, the need for construction contractors to adapt their insurance to a new market arises from the different risks posed by the rules and regulations surrounding construction, these risks being interrelated with: the types of construction materials used; the certification behind those materials; and the safety culture of the member state's construction sector (e.g. risk prevention methods). For this reason, Insurance Europe maintains that, similar to the legal profession discussed in Section 8, the issues discussed in Section 9 on construction do not arise from differences in insurance contract law.