

The Insurance Institute of Ireland
Annual Dinner
Rosslare

18 May 1979

EMBARGO: 18/5/79:20h30 (Brussels time)

INSURANCE POLICY IN THE EUROPEAN COMMUNITY AND
SOME IMPLICATIONS FOR CONSUMER AFFAIRS

Address by
Richard Burke
Member of the Commission
of the European
Communities

INTRODUCTION

It is a pleasure and an honour for me to have the opportunity of addressing you on the subject of insurance, its problems and opportunities, as seen from the standpoint of a Member of the Commission of the European Communities.

Insurance, in a sense, reminds me of taxation, for which I hold responsibility in the Commission. I hope you will not find the comparison odious. Both insurance and taxation are regarded by ordinary people as technical, complicated, hard to understand and full of small print. They are considered at best to be necessary evils. No doubt most of you in the present gathering will think of insurance as being considerably more necessary and considerably less evil than taxation!

INSURANCE AND CONSUMERS

Insurance is, of course, a major industry which employs many thousands of people, handles huge sums of money, is responsible for important investments, is one of the main channels through which savings are made and by its services helps to keep the wheels of commerce turning. It is also something which very much affects the man in the street because so very many people are, in one way or another, customers of insurance concerns - consumers, if I may put it that way, of insurance products. This aspect is very clear to me as Commissioner responsible for Consumer Protection.

.../... Insurance is not just

Insurance is not just a matter of covering major industrial risks or supertanker disasters - although what happened in Bantry Bay should remind us that these things are not necessarily as remote as we should like - but also concerns the security of farmers and shopkeepers, homeowners and motorists, and the savings of the elderly.

I mention this because much of what I have to say is concerned with the creation of a genuine common market in insurance within the European Community and has to do with the obligations and opportunities for insurance companies working across national frontiers. It is easy to think of insurance as being just a matter of big business, but we must never forget that it has effects on the everyday lives of ordinary people and that both the industry and the Community have a responsibility in this respect. I shall return to the subject of consumer protection in a more general sense later on.

COMMUNITY PROCEDURES.

I expect that all of you have some idea of the way in which the Community Institutions work and of the procedures entailed in bringing a Directive into being and putting it into effect. The inception of an idea is followed by much consultation with representatives of the Governmental Administrations of the Member States - consultations with bodies representing the industry at the European level, such as the Comité Européen des Assurance (in which of course, Irish representatives participate), and among Members of the Commission.

.../... Finally the stage

Finally the stage is reached at which the text of the proposed Directive is formally adopted by the Commission. That is by no means the end of the road. The proposal for a Directive is sent by the Commission to the Council of Ministers, which will seek the opinion both of the Economic and Social Committee and of the European Parliament. Irishmen are represented in both these bodies. When the Economic and Social Committee and the Parliament have given their opinions, the proposed Directive is subject to further detailed examination in a Council working group, in which, of course, Ireland is represented just as are the other Member States. And finally, when agreement is reached, the Directive is adopted by the Council of Ministers. After this, there will normally be a time lag - in complicated matters like insurance it may be several years - before the Directive has to be transposed into national law.

My reason for reminding you of this procedure is twofold. Firstly, I should like to emphasize that a very long time elapses between the first launching of an idea and its transformation into legislation that affects insurance operations. The First Non-Life Co-Ordination Directive, for example, started going through this process long before Ireland became a Member of the Community, and was adopted by the Council in July 1973. But because of the time lag to which I referred, it was not until 1976 that its provisions had to be enforced. There are other measures which will affect the insurance industry in Ireland at different points ^{stages} in the procedure I have described. When we think of Directives, we must remember that the future has its roots deep in the past.

The length of time needed to get anything done is, you may well think, a very negative aspect of Community affairs. But linked with it is a positive aspect. That is that there are so many stages at which the views of the industry can be brought to bear. This is true at the political and administrative level; it is true also of the insurance industry - the brokers as well as the insurers - and it is true of policyholders large and small.

So although Ireland is a small country, with not so very much more than 1% of the total population of the Community, there is no danger that its interests will go unnoticed. The procedures are there for making clear the special nature of Ireland's industry, and full use has been made of them. Nobody at the Community level who is concerned with insurance is unaware that, for historical and geographical reasons, a much larger part of the Irish insurance market is held by firms which are not based within Ireland than is the case with any other Member State. They know too that this starting position raises apprehensions. The fear is that a sudden removal of obstacles that at present prevent the effective exercise of the right to provide insurance services across national borders without the need to be established in the country concerned, would wipe out the Irish insurance industry. These fears may be exaggerated. Indeed, looking at the stalwart company assembled here this evening I cannot help thinking that the Irish insurance industry would not be without resource in such a situation and may derive some profit from it. But we in the Commission know the concerns of the Irish industry as do the other Member States. They cannot be ignored.

BASIS OF INSURANCE DIRECTIVES

It is equally important, however, to realize that what the Commission is proposing in its main programme of Directives in the insurance field, is something that derives directly from the Treaty of Rome and is therefore part and parcel of the terms that Ireland made when she decided to join the Community.

In the insurance area, we are concerned with two basic freedoms both of which are laid down in the Treaty of Rome. These are the freedom of establishment - the right, that is, to set up business (whether a new business or the extension of an old one) in any Member State in the Community - and the freedom to provide services from a base in one Member State to a recipient of those services in another Member State. These freedoms are now absolute rights - if we are to judge from decisions of the European Court of Justice. No Member State may refuse the exercise of either of these freedoms to anyone from within the Community on the grounds of nationality or national residence.

What this actually means in practice is something which is only gradually emerging as the Court hands out further judgements. As yet there has not been any judgement concerning these basic principles in the area of insurance, although certain decisions given recently seem to have a close bearing on insurance matters. One thing is clear. It does not mean that an insurance undertaking in one Member State can operate in another Member State with complete disregard for that State's laws.

.../... But it does mean

But it does mean that national laws which restrict the exercise of the freedoms in question are liable to be called in question unless they can be shown - as the Court would say - to be "objectively necessary". Objectively necessary, that is, in order to protect the interests of the citizens whose importance I have already stressed, and not in order to protect the interests of the insurers.

What is "objectively necessary", in this sense, in the world of insurance? One thing that has always seemed fairly certain is that the people who want to insure large industrial risks have a less obvious claim to protection than the small man and above all than the person who takes out a life assurance policy. But little else is certain. In this situation the Commission cannot leave everything to the Court but has the very clear duty to bring about a basic co-ordination of the control measures applying to insurance undertakings in the various Member States, especially as regards the financial guarantees that are required of them. Only in this way can the basic freedoms enshrined in the Treaty be given their full effect.

INSURANCE DIRECTIVES

It was agreed between the Member States long before Ireland joined the Community that these necessary co-ordination control measures had to proceed by two stages. The co-ordination needed for the right of freedom of establishment had to come first, to be followed later by the further co-ordination needed for the freedom to provide services. Within each

of these two stages it was agreed to deal with non-life business first and afterwards to go on to life assurance.

Thus we have the First Non-Life Co-Ordination Directive, which was proposed by the Commission in 1966 and adopted by the Council in 1973. As I mentioned earlier, it has now been in force for over three years. This was followed by the First Life Co-Ordination Directive, submitted to the Council by the Commission after much preliminary work, in 1973, and adopted by the Council in March of this year. Member States have eighteen months in which to amend their legislation to give effect to the provisions of this Directive and then another eighteen months to put the law into effect.

Next we have the Second Non-Life Co-Ordination Directive, better known perhaps as the "Services Directive". This second Directive will, when adopted by the Council, remove the obstacles that at present impede the provision of non-life insurance services across many of the national frontiers within the Community. It will do so at least as far as major industrial risks and international transport risks are concerned, though just how far it will go is something that remains to be seen.

The next stage should logically be the submission of a Second Life Assurance Directive, which would do for freedom of services in the life assurance field what the so-called Services Directive is intended to do on the non-life side; but you will not be surprised to learn that this latest potential offspring is still at a very early stage within the Commission.

You will also be aware of the Co-Insurance Directive, which was adopted by the Council in the Summer of 1978 but which has not yet come into force. It fits into the picture as a sort of precursor, in a limited area, of the main Services Directive, and as such forms part of the general plan I have outlined.

The First Non-Life and the First Life Directives have many points in common - not surprisingly, as they share a common goal in their respective fields.

Each provides that Member States shall make the taking up of business in its territory subject to official authorization. Conditions for the granting of the authorization are laid down ^{for} by Head Offices and also for Branches and Agencies. If they are fulfilled, authorization cannot be refused, provided that the insurance undertaking is based in the Community.

The supervisory authority of the Member State in whose territory the Head Office is situated is responsible for the state of solvency of the undertaking as a whole, and rules are laid down concerning the necessary solvency margin.

On the other hand, the supervisory authority of each Member State in whose territory the undertaking carries on business, whether through its Head Office or through a Branch or Agency, is responsible for seeing that the insurance concern in question establishes sufficient technical reserves, including mathematical reserves, and it does so in accordance with its own rules or practice.

This is as far as co-ordination needed to go in order to achieve the necessary removal of obstacles to the freedom to establish within any particular Member State. What is secured is equal conditions of competition within each national market, regardless of the country of origin of the insurer, in accordance with rules that are still largely national in nature.

But it is obviously necessary to go further than this in order to achieve the true fusion of the national markets that has to come about if there is to be real freedom to exercise services in one country from a base in another country. It is this further co-ordination that the Second Non-Life Directive, otherwise known as the Services Directive, seeks to achieve, and it is appropriate that at this particular time and in Ireland I should say a little about the problems that remain to be overcome, because Ireland will, of course, be assuming the mantle of the Presidency of the Council of Ministers for the six months that will begin on 1 July and will have the task of leading the work on this Directive in the Council groups during this period.

The Directive was proposed by the Commission to the Council in 1975 but was resubmitted in a modified form in February 1978, the modifications taking account of suggestions made by the Economic and Social Committee and the European Parliament. Little work was done on this Directive in the second half of 1978, because all efforts were concentrated on the First Life Assurance Directive. In the first half of 1979, however,

the French Presidency has set a tremendous pace of work in the Council working group.

The main problems which still remain outstanding, although they have been debated to a greater or lesser extent already, are the following.

Shall there be a free choice of national law applicable to an insurance contract in all cases, in some only, or in none? If Member States are left free to make up their own minds on this, would a country such as Ireland that has traditionally had free choice of law suffer a competitive disadvantage as against others that take a restrictive view?

Can the freedom of services with which we are concerned be exercised only by a Head Office, or is it rather, as the Commission thinks, that this freedom can also be exercised through Branches and Agencies? How can the line be drawn between business that is done through an establishment (a branch or agency) and business that is done in full freedom of services? In other words, how can we define Branch or Agency?

Are certain provisions of the Directive to apply only to major risks - and if so, how are major risks to be defined?

What can we do to bring about a basic harmonization of technical reserves? Do we, for example, want equalization reserves and, if so, on what basis?

.../... What about premium

PRODUCT LIABILITY.

A Commission proposal which will have important implications for insurers is the directive on Product Liability. The aim is to introduce a standard of strict liability for defective products. The underlying idea is that the producer has a responsibility for the products which he has put into the stream of commerce. He is the best person to shoulder the burden of providing compensation to consumers who have suffered damage, loss or injury as a result of defects in those products. He can do so by taking out product liability insurance and spreading the cost over all of his products. Ultimately, the consumer will pay for this extra protection. It will be included in the price of the items he buys. However, most indications seem to show that the increased cost will not be excessive.

The Commission's proposal has recently been approved, subject to a number of amendments, by the European Parliament.

Commission proposals for the harmonization of laws, and the product liability directive is one such, are submitted to the Economic and Social Committee and to the Parliament. The Commission is not bound by the opinion of the Committee, nor by the resolution of Parliament, but they create part of the dynamics of the situation in which Community decisions are made. This is the push and pull which shapes Community decisions. Another part of the process are the views expressed by consumer, commercial and industrial organisations, who represent specific interests and command respect, even though they have no official status.

What about premium taxes, which are applied in most Member States but not in Ireland or the United Kingdom? Can they be brought into line or should they be replaced by Value Added Tax - as some wish - or can they simply be left as they are?

All these are questions which still have to be finally resolved. Rather a formidable list, you may well think.

However daunting the list of problems may appear, we should not give up hope. Equally daunting problems have been overcome in the past in connection with the Directives that have now been adopted by the Council. Moreover, one thing without which no real progress can be achieved, but with which a very great deal is possible, already to a large extent exists. I am referring to the co-operation between the supervisory authorities which is the very cement of the entire system which we are trying to build. In this, Ireland has played a very full and constructive role; and I feel sure she will continue to do so.

A good illustration of this dynamic process in operation is to be found in the product liability directive. As originally proposed by the Commission, it created liability for development risks. Thus the Commission's original proposal was that products which were defective as a result of faults in design or development or errors in research could give rise to liability on the part of the producer, if the defect caused damage, loss or injury. The Commission proposed that this should be so even if the producer could not have known that the defect existed, let us say, where the state of the art was insufficiently advanced to enable him to do so. This approach has caused very grave concern to industry. It has been said that this rule would deter and inhibit innovation; that it would lead to increased prices and even to a reduction in employment by industrial firms.

For consumers, the inclusion of development risks within the strict liability envisaged by the product liability directive was one of its essential features, particularly after so much attention had been focussed upon the terrible consequences for consumers of development failures by industry. One has only to think of the thalidomide case. Nobody can measure the untold misery introduced into the lives of those poor, malformed children whose mothers had been unfortunate enough to have prescribed for them the drug thalidomide. And I would ask you to note particularly that the drug was prescribed for them. These women were not exercising their own judgment or a free choice in the matter. They took what they were given and the consequences were appalling. Another example of the distressing

consequences for consumers from what appears to have been a development fault was the DC-10 crash at Orly airport in 1974. Nearly 350 people were killed when the door of the baggage compartment imploded as a result of pressure equalisation when the aircraft climbed. Yet again a case in which consumers take on trust the manufacturer's product. They really have no means of knowing whether it has been properly designed and the difficulties of proving a design fault after the event are immense.

I know that some people will say that the certification by public authorities of such products as pharmaceuticals and aircraft should be the consumers' guarantee. But it is not enough in itself. It provides no compensation for those who have suffered and, in a caring society, they ought to have compensation. It is only right where loss or injury has been caused by a defective product, that the producer of that product should bear responsibility. He is in the best position to cover the risk. Product liability insurance is available, as insurers have confirmed, even to cover development risks.

What sort of burden will this place upon industry? It is absolutely clear that certain industries will not be affected at all. Manufacturers of stationary, manufacturers of clothing, or of furniture, will not feel the impact of this product liability directive. Certain other industries will feel it, pharmaceuticals and aviation are prime examples. Nevertheless, even in these cases, one must keep a sense of proportion. Many products of these industries had been in existence for a number of years. Their characteristics are well known.

Any problems which may have existed have been ironed out. Newly developed products are very often based on existing products. The new developments do not constitute a step into the unknown. I suppose the real risk is centered on totally new developments. But is it not right that a producer who puts a totally new product on the market should take special care and caution in the development process and in the quality control for that product? In that respect, the product liability directive, if it includes development risks, will provide a powerful incentive to the manufacturer.

I understand the very genuine concern of industry over the increased burden which the directive will impose. At the same time, industry's fears have been exaggerated. There have been scare stories from the United States, where strict liability already exists. Many of these stories have been apocryphal. What is more, the legal system in the U.S. is different from that of the Community and its Member States. In the U.S.A., lawyers operate upon a contingency fee basis, often in class actions, so that the plaintiff can chance his arm without too much care for the costs of litigation. In the U.S.A., damages are awarded by juries. Only in Ireland is that the case within the Community. In the U.S., penal damages may be awarded where a manufacturer has been at fault. This is unknown in personal injury claims within the Community. The experience of the U.S.A. is a poor guide on the question of the consequences for industry of product liability.

16

But the Commission does not want the product liability directive to have an unlimited impact on industry. It has been our task to balance the interests of industry on the one hand and consumers on the other. For that reason we have included in the product liability directive a financial limit on liability. And it is my considered opinion that within the limits proposed, the additional responsibility which would fall on industry under the proposed directive should be acceptable.

Parliament, on the other hand, has considered the Commission's proposal too strongly worded in favour of the consumer. It has proposed that development risks should be retained, while creating a state of the art defence. In other words, the producer will have a defence if he can prove that the article could not be considered defective in the light of scientific and technological development at the time when the article was put into circulation.

That is how matters stand at the moment. The ball is now back in the Commission's court, and the Commission will have to decide how it is to proceed. Parliament's solution will certainly not satisfy most consumers. BEUC, the European Office of Consumer Unions, has greatly regretted the amended rule for development risks. Nevertheless, the function of the Commission in these matters is to strike the best possible balance of interests and not to allow any one interest, even that of the consumer, to become paramount.

In reaching its decision, the Commission will probably have to consider alternative solutions. One has been given prominence in the second paragraph of the European Parliament's Resolution. It requests the Commission to report on the advisability of covering liability for defective products out of a guarantee fund. This would be wholly subscribed by governments or contributed to by industry, particularly with a view to protecting consumers against development risks. But that is another story.