European Integration Reassessed: A Grounded Theory Approach

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ABSTRACT

This thesis investigates the mechanics and predominant theories (neo-functionalism and intergovernmentalism) at work in the process of European integration. Indeed, it provides an illustration of the difficulties in achieving the harmonisation of Member State legislation and identifies the intricacies and practicalities of successful decision-making in the European Union (EU). In the aftermath of the Single European Act (SEA), the beginnings of the Single European Market (SEM) and the Maastricht Treaty, it has become evident that financial service sectors need to involve themselves in the creation of the EU.

Through grounded theory methodology, an empirical study of the European life insurance industry in general and of the Third Life Assurance Directive in particular, this thesis investigates the extent of sector involvement in the EU's decision-making processes and in doing so, critically analyses theoretical understandings of European integration. Grounded theory methodology is illustrated by the thesis in the following ways. First, through a comparative analysis which was achieved through the open coding (conceptualisation, categorisation and dimensionalisation) of individual Member States' life insurance regulations. Open coding leads to the formulation of a regulation table and matrix. Further coding, through a survey of Member State life insurance industries, refined and verified the matrix. This investigation raised questions as to how the legislative differences (that underpin regulatory structures) between Member States may be resolved. Secondly, through an interview programme, process was verified and illustrated through a series of models. The tables, models and the matrix provide the building blocks of the substantive theory. Thirdly, axial coding is illustrated by the matrix and models fitting together around the core category of European integration. The core category was identified through selective coding and is the category around which sub-categories are integrated. Axial coding draws all parts of the analysis together: it is the pivot or the axis of theory building. Finally, substantive theory is formulated through grounded theory techniques in relation to the formal theories of neo-functionalism and intergovernmentalism; this allows a reassessment of European integration and provides a clearer understanding of the formal theories.

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List Of Abbreviations

ABI	Association of British Insurers
BIIC	British Insurers International Committee
BIPAR	Bureau International des Producteurs D'Assurance et des Assurances
CAP	Common Agricultural Policy
CEA	European Insurance Committee
CET	Common External Tariff
COREPER	Committee of Permanent Representatives
DG	Directorate General
DTI	Department of Trade
EC	European Community
ECB	European Central Bank
ECOFIN	Council of Economic and Finance Ministers
ECSC	European Coal and Steel Community
Ecu	European Currency Unit
EDC	European Defence Community
EEC	European Economic Community
EFTA	European Free Trade Area
EMI	European Monetary Institute
EMU	Economic and Monetary Union
EP	European Parliament
ERM	Exchange Rate Mechanism
ESCB	European System of Central Banks
EU	European Union
FIMBRA	Financial Intermediaries Managers and Brokers Association
GATT	General Agreement on Tariffs and Trade
GDP	Gross Domestic Product
GNP	Gross National Product
IGC	Intergovernmental Conference
LAUTRO	Life Assurance and Unit Trusts Regulatory Organisation
MEP	Member of the European Parliament
NATO	North Atlantic Treaty Organisation
NTB	Non-Tariff Barrier
OCA	Office De Controle des Assurance
OCI	Officer of the Commission for Insurance
OJ	Official Journal of the European Communities
PIA	Personal Investment Authority
QMV	Qualified Majority Voting
SEA	Single European Act
SEM	Single European Market
TEA	Treaty on European Union
UK	United Kingdom
UN	United Nations
WTO	World Trade Organisation

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For Clare

Introduction and Overview of Thesis

No conclusion of peace shall be considered valid as such if it was made with a secret reservation of the material for a future war (Kant, 1995; p 95).

Introduction

From the late 1960s until the mid-1980s when one discussed European integration one usually emphasised intergovernmentalism. "Neo-functionalism and intergovernmentalism were contending theories of European integration in the 1960s but by the 1970s intergovernmentalism appeared to have carried the day, until in the 1980s the single market programme and the Single European Act led to a revival of neo-functionalist explanations" (George, 1994; p 1). This thesis wishes to enter the debate and seeks to illustrate the extent to which neo-functionalism or intergovernmentalism may be at work in the process of European integration. An analysis of a service sector (the life insurance industry) has been undertaken in respect of its relationships with the EU decision-making institutions. It is considered that through *self-interest*, national life insurance industries attempt to create a market in their own image. Through compromises, a single market is formed, European integration taken a step further and this enhances the welfare of Europeans in general. Fundamentally, in the perpetuation and evolution of the human species, *self-interest* and *mutual assistance* work hand-in-hand.

Open coding began with a series of preliminary interviews with UK life insurance companies and the Association of British Insurers (ABI) and a comparison of Member State life insurance legislation and regulation. This

gave an idea of the UK sector's general understanding of Europe and allowed the compilation of a questionnaire. Interviews were later undertaken in Brussels, Paris and London where individuals involved in the decision-making processes were asked to comment on their part in the creation of the Third Life Assurance Directive.

A major survey of the European life insurance industry provides an understanding of that industry in terms of how it approaches the EU, how it ascertains national self-interest in terms of market conditions, and the extent of compromise in the creation of the Single European Market (SEM). Less extensive surveys were made of European and national interest groups, the European Parliament and Permanent Representatives.

Inductive investigation allows an overall picture of the EU and SEM to be established; subsequently this allowed deductions about the European integration process. Through the induction-deduction aspects of grounded theory methodology, further understanding of European integration is established.

The thesis explores whether the EU is *supranational* and whether this supranationality, in tandem with *spillover*, is part of the integration process. European integration is worth revisiting because of the renewed pace of the integration process, impending monetary union and the implications this has for political union. Additionally, the thesis questions how far interest groups and industries are either the willing or unwilling creators of European economic and political union and to what extent *self-interest* creates peace and welfare in Europe and ultimately the Kantian 'civic constitution'? Indeed, because of the renewed pace of European integration theoretical explanations need to be reassessed.

Neo-functionalism went into decline with the slowing up of the integration process. Now the pace has quickened, it may be possible to discern elements of neo-functionalism, in relation to intergovernmentalism, at work in the evolving SEM and EU. This thesis intends to determine the extent of neo-functionalism in the re-vitalised European integration process. Keohane and Hoffman (1990) emphasised the need for a theoretical framework for the evolving EU and indicated that neo-functionalism may provide this. However, they do point out that further empirical research is necessary. This thesis wishes to provide a part of that research.

An Overview of the Thesis

The thesis is divided into nine chapters. The introduction outlines the thesis in terms of the philosophical and theoretical bases of the proposed analysis and provides an overview of the thesis.

Chapter One provides the literature review: this covers the methodology (grounded theory); the political philosophy of Kant; integration theory (specifically functionalism, neo-functionalism and intergovernmentalism); and the life insurance industry and the EU.

In Chapter Two, the methodology (grounded theory) is explained in line with the concept of *self-interest* and *mutual assistance*. In previous studies of neo-functionalism, the problem of a dependent variable and the charge of Eurocentricity have been major criticisms. This thesis recognises these deficiencies but wishes to look at neo-functionalism and integration theory in a different way. Initially, through inductive and later deductive procedures, a substantive theory is constructed through which our understanding of neo-

functionalism, intergovernmentalism and the European integration process may be enhanced. The methodology considers that the most important aspect of research is not explanation but understanding. Thus, the thesis does not wish to prove or disprove neo-functionalism nor intergovernmentalism: it simply wishes to comprehend them as theoretical frameworks and consider how they may further our understanding of the European integration process. As acknowledged above, the thesis also recognises the deficiencies of neo-functionalism and intergovernmentalism in respect of their application to the EU alone (or Eurocentricity) and considers that in this context they are substantive theories themselves[1].

Initially, Chapter Three furthers the discussion regarding theory initiated in the methodology chapter. Through this discussion, it challenges some of the past criticisms of integration theory in general and more specifically functionalism and neo-functionalism. Additionally, it provides an analysis of integration theory, by comparing functionalism and federalism and illustrates how neo-functionalism is linked to and affected by these. Indeed, it posits that a number of aspects of functionalism and federalism make up neo-functionalism. It also investigates the links between realism and intergovernmentalism. Finally, it considers whether these theories are underpinned by Kantian political thought. The chapter illustrates the complexity of integration theory and its relationship with the five main theoretical schools. It considers that functionalism is peace-oriented and has much to teach us about non-violent means of solving international problems. Indeed, the chapter concludes that the EU decision-making process, through the use of interest groups, is a means of overcoming turbulence and consequently steps up political integration. This is taken further in Chapter

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[1] Substantive theory is built through grounded theory processes to allow an analysis and further the understanding of neo-functionalism and intergovernmentalism (or formal theories) in the process of European integration. Both substantive and formal theories are defined further in the methodology chapter below.

Four where an analysis of neo-functionalism and intergovernmentalism is undertaken.

Chapter Four analyses intergovernmentalism and neo-functionalism in more depth and contends that in the aftermath of the Single European Market (SEM) and with the possibility of European Monetary Union (EMU), European integration should be reassessed. On the one hand, intergovernmentalism argues that inter-state agreements underpin the conditions necessary for European integration, i.e. that the primary source of integration is to be found with the Member States. On the other hand, neo-functionalism considers that integration involves the transfer of allegiance by political actors to a supranational entity and this provides a major impetus for European integration. Just as functionalism can be identified as being premised on peace, neo-functionalism can be considered a peaceful process toward the creation of larger peaceful political communities, i.e. a peaceful process aimed at a peaceful outcome. The concepts of spillover, supranationalism and the uses of sub-national actors are identified and critically evaluated. Finally, the chapter posits that neo-funtionalism and intergovernmentalism are not incompatible in understanding European integration and that this may be explored through empirical investigations. This is what the rest of the thesis sets out to accomplish.

Chapter Five provides the foundations of the substantive theory through the construction of a regulation matrix. The chapter builds on the grounded theory techniques of *categorisation*: and *dimensionalisation* defined in Chapter two (see Table 2.1 p 43) and further illustrates the differences between Member State life insurance industries' regulation and legislation. The matrix posits convergence which illustrates the creation of an SEM through harmonisation. To the initial coding the results of a survey are added. The

survey allows *verification* through the use of frequency tables, cross-tabulations and chi-squared tests. The formulation of Tables 2.1 and 5.1 (p 43 and p 138) and Figures 5.1 and 5.2 (p 157 and p 160) provide the initial stages of the substantive theory and set up a number of questions that are addressed in the following chapters.

Chapter Six looks at interest groups and the supranational aspects of the EU decision-making institutions. As identified in Chapter Three, these are two major provisions in allowing a neo-functional understanding of European integration. Interest groups are defined as non-governmental bodies that attempt to influence the policies of public institutions i.e. as entities that apply pressure. Interest groups can be either sectional or promotional. However, this thesis concentrates on the sectional interest groups in those of the life insurance industry. Lobbying in Brussels is open to uncertainty: consequently, co-ordination and alliances with European counterparts are extremely important interest groups are to be successful. The discussions in relation to the legislation and regulatory regimes that should be pursued to create the most amenable regulatory structure for all Member States are monitored and commented on.

Chapter Seven amends Easton's demand model (1965) and constructs a decision-making model. The demand model illustrates how interests, preferences etc, transform into demands at the EU level and adds to the substantive theory in abstract terms. The decision-making model, developed with the aid of a number of key player interviews (Richards, 1996), adds to the substantive theory in more concrete terms. The interviews were undertaken with individuals involved in the creation of the Third Life Assurance Directive and provide an understanding of the EU decision-making processes.

They also give some insight into the formal theories of intergovernmentalism and neo-functionalism.

Chapter Eight generalises the process indicated in Chapters Five, Six and Seven. It considers the concept of spillover and the part this plays in the process of European integration. The chapter adds to the substantive theory through the construction of a spillover model which provides an understanding of spillover processes in the EU. The chapter investigates spillover and asserts that it plays a part in the creation of the SEM in financial services. This is accomplished through an analysis of EU financial services legislation. The chapter considers that there are delineations between horizontal and vertical spillover[2] and intergovernmental and neo-functional spillover. It also contends that the revival of supranationalism has given an impetus to the integration process that spillover creates. Additionally, the part life insurance plays in the process of integration, and the difficulties in creating the Third Life Assurance Directive are illustrated. The chapter concludes that the integration of financial services is intrinsically tied to the success of EMU, and that even though neo-functional spillover is an important process it can only take European integration so far without further intergovernmental spillover in the form of further treaties.

Chapter Nine sets out a substantive theory which illustrates the extent to which neo-functional and intergovernmental processes are at work in the process of European integration and how far sectors, through interest groups and the Commission, dictate the pace of integration. Additionally, there is a questioning of intergovernmentalism and nationalism and the extent to

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[2] Neo-functional spillover is part of the integration process in that legislation in one area spills into another either vertically (in the same industry/sector); or horizontally (from sector to sector). Furthermore, intergovernmental spillover also exists. This is where one treaty necessitates further treaties and where the neo-functional process pushes for further integration through the harmonisation of specific legislation which will eventually necessitate further treaties (see Chapter Four, Chapter Eight and the Spillover Model, 277-81)

which these accepted norms are historical realities. The research questions these historical constructs and posits that they are relativist entities that are being surpassed by larger political communities which in themselves are part of a general process of integration. Finally, the work will add to the understanding of integration processes in a regional setting, i.e. European integration.

Chapter One

Literature Review

> *The ultimate philosophy and the hierarchy of preferences invite discussion rather than proof or refutation; analyses of present facts or prognostications about facts to come, alter with the unfolding of history and the knowledge we acquire of it (Aron ,1985; p 236).*

Introduction

This chapter overviews the literature that the thesis has drawn on while building a substantive theory and an understanding of European integration processes. The literature review is broken down into three areas, each of which interacts with the others to provide the overall underpinning of the thesis. The areas incorporate: the methodology literature; integration theory literature; and life insurance and European Union literature. The subject areas are covered in the order they appear in the thesis.

Methodology Literature

Grounded theory suggests that there is an over-emphasis on verification theory and wishes to demote the idea that the discovery of relevant concepts and hypotheses are *a priori* to research (Glaser and Strauss, 1967; Glaser 1978; Charmaz, 1983; Strauss, 1987; Strauss and Corbin, 1990; Corbin and Strauss, 1990; Glaser 1992; Strauss and Corbin, 1994; Stern, 1994; Melia, 1994; Annells, 1996).

Glaser and Strauss (1967) draw on the pragmatist school, particularly Dewey (1950) and Mead (1962). Dewey (1950) considered that theory cannot answer questions ". . . unless we are willing to find the germs and roots in matters of experience" (p 12). Furthermore, grounded theory can be based on *symbolic interaction* (Mead, 1962) and Blumer (1962; 1969). Symbolic interaction is distinct to human beings, it is part of what makes us human because we ". . . interpret or define each other's actions" (Blumer, 1962; p 179) rather than simply reacting to them. Furthermore, humans have and are able to act towards self . Mead considered that the ability to react to self was the central mechanism of existence.

> This mechanism enables the human being to make indication to himself of things in his surroundings and thus to guide his action by what he notes. Anything of which a human being is conscious . . . he is indicating to himself . . . The conscious life of the human being . . . is a continual flow of self indications (ibid p 180).

Fundamentally, ". . . the formation of action by the individual through . . . self-indication always takes place in a social context" (ibid 183).

> One now regularly takes an impartial and general standpoint in observing and evaluating one's own conduct . . . (however) . . . The organised community or social group which gives to the individual his unity of self may be called the generalised other which is the attitude of the whole community (Blau, 1952; pp 162-163 authors brackets).

Symbolic interaction presupposes the following:

(a) the individual has a self and an amalgamation of interpreted selves encompass society;
(b) individual action is constructed through interpreting the situational context;
(c) groups and collective action incorporate the alignments of individual actions that are formulated through interpreting the actions of others.

Consequently, research should be pursued with this in mind, interpretations of situations change as individuals change (this includes the researcher and the researched). Indeed, with the knowledge that pure objectivity cannot be attained the research may be more objective i.e. any analysis that does not accept subjectivity can never be objective. Grounded theory attempts to understand social patterns on the basis of symbolic interaction and construct social theory.

Grounded theory looks to the generation of theory through comparative analysis and does not attempt to undermine theory but to better it. Effectively, "... a theory's only replacement is a better theory" (Glaser and Strauss, 1967; p 28).

> Grounded theory is based on the systematic generating of theory from data, and itself is systematically obtained from social research. Thus the grounded theory method offers a rigorous orderly guide to theory development that each stage is closely integrated with a methodology of social research" (Glaser, 1978; p 2).

Fundamentally, research should be approached with an open mind and as much objectivity and distance as is possible. However, it is acknowledged that such objectivity is difficult, as everyone has subjective tendencies. Yet recognising subjectivity is part way to overcoming it. This may be considered to encompass theoretical sensitivity which is initially gained by entering the research ". . . with as few predetermined ideas as possible, especially logically deduced, *a priori* hypotheses" (Glaser, 1978, p 3). Such enables the researcher to remain sensitive and ". . . record events and detect happenings without first having them filtered through and squared with pre-existing hypotheses and biases" (ibid).

This, one may consider, is what may be labelled foresight or that which allows the researcher certain expectations of what may be discovered. As does the background or environment (fore-structure) which indicates possible ways of questioning (Heidegger, 1978). Additionally, Stern (1994) considered that grounded theory was an interpretative method and was underpinned by ". . . phenomenology, that is methods that are used to describe the world of the person or persons under study" (p 213).

Guba and Lincoln (1994) consider that grounded theory is *postpositivist*, while, Annells (1996) contends that our understanding of grounded theory is based on an ". . . awareness of the method's ontological, epistemological and methodological perspectives" (ibid; p 379) and that these may be broken down into four paradigms of enquiry. These are *positivism, postpositivism, critical theory* and *constructivism*. Indeed, that one's understanding of methodology and consequently grounded theory is determined by one's metaphysical assumptions. Grounded theory involves the ". . . soliciting of emic viewpoints to assist in determining the meaning and purposes that people ascribe to their actions" (Guba and Lincoln, 1994; p 110).

> Grounded theory methodology incorporates . . . assumption(s) . . . concerning the human status of actors whom we study. They have perspectives on and interpretations of their own and other actors' actions. As researchers we are required to learn what we can of their interpretations and perspectives" (Strauss and Corbin, 1994; p 280 authors brackets).

This thesis considers that this is the basis of grounded theory: an attempt to understand reality through social constructions and an attempt at objectivity through recognising the subjectivity of the researcher and researched in terms of their interpretative nature.

Integration Theory Literature

The main aim of this thesis is to reassess the main theories of European integration; neo-functionalism and intergovernmentalism. It is considered that the former of these grew out of the Kantian concept of the international civic constitution (Kant 1995, see *Idea for a Universal History With a Cosmopolitan Purpose* pp 41-53 and *Perpetual Peace* pp 93-115) and the latter through the Hegelian concept of the state (Hegel, 1967). Indeed, both are based on Enlightenment thought in general. However, the roots of the ideas of integration may be identified in Aristophanes (1970). In his play, the Goddess, Peace is released from the pit by the "farmers, merchants, labourers, craftsmen, aliens, visitors . . . Now if ever panhellenic let us help each other out" (pp, 233-34). Peace is buried deep but through working together, through the integration of activity, Peace is be freed from her pit. This identifies neo-functionalism: a peaceful means in the pursuit of a peaceful end. Additionally, in reassessing European integration, it is necessary to examine

the extent of neo-functionalisms main theoretical disputant, intergovernmentalism, the basis of which is grounded in realism (Morgenthau, 1973).

There have been a number of commentators who have written in the realms of integration theory and discussed how it relates to federalism functionalism, intergovernmentalism and neo-functionalism (Bulmer 1993; Claude 1956; George 1994, 1995; Groom and Taylor 1975; Haas 1958, 1964, 1968, 1971, 1975, 1976; Heathcote 1966; Hoffman 1966; Keohane and Nye 1990; Keohane and Hoffman 1990, 1991; Lindberg 1963 1967; Lindberg and Scheingold 1970, 1971; Moravsik 1991, 1993; Mitrany 1943, 1944, 1965, 1970, 1975, 1975a, 1975b, 1975c; Nye 1971, 1971a; Pentland, 1973; Rees 1992; Sandholtz and Zysman 1989; Sandholtz, 1994; Schmitter 1969; Schmitter and Streeck, 1994; Sewell 1966; Sweeny 1984; Taylor 1968, 1968a, 1983, 1971; Wallace, Wallace and Webb 1977; Wallace 1990; Webb 1983). However, in general the debate revolves around neo-functionalism and intergovernmentalism and which of these is most precise in describing the process of European integration.

The initial proponents of neo-functionalism were Haas (1958) and Lindberg (1963). However, they were both to reconsider their understandings of neo-functionalism because of the re-assertion of the nation-state in the 1960s. Indeed, the actions of De Gaulle illustrated the deterministic nature of neo-functionalism and the absence of a dependent variable[1] (Heathcote, 1966). This led to ten years of debate and the temporary displacement of neo-functionalism. Yet, because of the impetus the SEA and the Maastricht Treaty created, commentators are once again turning their attention to neo-

[1] The dependent variable regarding European integration relates to some sort of end result. Neo-functionalism does not propose an end. It does not draw borders around Europe nor give it a specific form. It is a peaceful process pursuing a peaceful end. However, the material aspect of the end is uncertain.

functionalism. Indeed, Rees (1992) commented that the recent developments in Europe ". . . have led to renewed interest in theories of integration, especially neo-functionalism" (p 13).

The modern understanding of functionalism[2], in the realms of international relations, is commonly attributed to David Mitrany. Additionally, the ideas of federalism[3] were re-formulated over the same period in history (see Bosco, 1991 and Hodges, 1972) and in themselves provide a strand of neo-functional thought[4]. The thesis provides an analysis of neo-functional ideas that emanate from functionalism and federalism. Functional theories have also been posited by Claude (1956) who builds on Mitrany's work (1943) and considers international organisation as a process; and Sewell (1966) who attempts to test the functional process through an analysis of the World Bank. Haas (1958) proposed a concept of incrementalism which was based on his study of the European Coal and Steel Community (ECSC); this placed an emphasis on 'functional integrationalism' (Burton, 1975). Out of Haas'

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2 Functionalism is the means by which change toward a goal of international collaboration is brought about; it is illustrated through organisations which would be designated a specific task that would evolve as functional needs changed. The system incorporates the premise of peaceful co-operation. The outcome may be a pluralist international community where national control is marginalised through functional linkages, or more extreme, where the nation-state disappears and is replaced by functional rationality. This is where organisational patterns are untertaken at the most rational level i.e. either continental, international or local. Effectively, functionalism is a process of internationalisation in terms of politics and the assurance of peace, whereas decisions, are carried out at the most rational or functional level. Functionalism does not adhere to the concept of constitution or regionalism. In Kantian terms, it pursues the concept of 'Perpetual Peace' without a civic constitution at a regional nor international level. Mitrany considered that human beings have no concept of what the end result of integration should encompass, so why invent one? Kant may be perceived as functionalist in terms of his pursuit of world government or internationalisation. However, he may be considered federalist in terms of his wish for a constitution.

3 Federalism, is based on the concept of peace and is premised on the Kantian ideas of both the civic constitution and 'Perpetual Peace'. Federalism may be understood in terms of the development of European history. Initially, it may be seen as an ideal denied by the nation state between the French Revolution and the First World War; secondly, the inter-war period where it allows an understanding of the European crisis; and finally in the post-war period where its application could overcome the European difficulties with the nation state and war. The difference between functionalism and federalism is that the former identifies a process: the latter an end result in the federal state. Federalism provides for the enlargement of representative government; it allows administration to extend from one to many states. (see Bosca, 1991; p 5). If one considers a world federation flowing out of European federalism then one may be indicating a neo-functional end in that supranationality is not an end in Europe but part of the process toward internationalisation.

4 Unlike functionalism, neo-functionalism posits that integration is most easily to be realised in a regional setting. Functionalists conceded that a supranational state would keep peace at the regional level. However, it would also create a power bloc and this would not ensure peace at the international level. In this context Mitrany criticised European integration. Haas accepted Mitrany's criticism when he wrote ". . .regional integration may lead to a future world made up of fewer and fewer units, each unit with all the power and self assertion that we associate with classical nationalism"(Haas, 1970). This relates to the difficulties created in terms of the lack of an independent variable. Neo-functionalism is the interaction between interest groups and the new supranational centres of power in the pursuit of a new market environment.

theories came an emphasis on neo-functionalism (Haas 1958, 1964, 1968, 1971). Puchala (1972) likens integration theory to the story of the blind men and the elephant: ". . . each blind man concluded that the elephant had the appearance of the part he touched . . . each had gained enough evidence from his own experience to disbelieve his fellows and to maintain a lively debate with his fellows" (ibid, p 267). Ultimately he posits a "concordance system", one in which actors find it possible to harmonise their interests consistently, from which an analysis of the dynamics of international integration may be launched (ibid, pp 276-283). Taylor (1968) contends that there are two broad theories for understanding Europe: (a) federalist/neo-functionalist (b) technocratic/functionalist. However, he does not come to any conclusions about which is the most useful, but he does clarify some aspects of integration theory. Nye (1971) considered that neo-functionalism should be used as a means of understanding integration and making comparisons: that if it is freed from the characteristics that linked it specifically to Europe, it would be useful for analysing integration in other settings.

Neo-functionalism has also been influenced by systems theory (Easton, 1953) and envisages elites and interest groups that change their loyalties towards a supranational grouping, rather than national groupings alone. This is done to satisfy wants, preferences and interests that transfer into demands which in turn are transformed into decisions (Easton, 1965). Lindberg acknowledges this approach to the extent that there is a process by which "political actors" in different settings ". . . are persuaded to shift their expectations to a new centre" (Lindberg, 1976; p 6). He considered that as

> . . . a contributor to the European integration literature I have more and more come to feel as if I were excavating a small

> isolated portion of a large, dimly-perceived mass, the contours of which I could not make out (Lindberg, 1967; p 345).

To overcome this Lindberg uses Easton's model (Easton, 1965a, 1965b) to provide ". . . a framework of logically consistent and integrated categories" (Lindberg, 1967; p 346). He concentrated on Mitrany's idea that there should be no end result to aim for, and omits any reference to a political community. However, in both Haas and Lindberg, there is a change of emphasis in respect of the institutions on which the interest group or sector makes its demands: in this context, the European Union.

Further understandings of neo-functionalism are based around Schmitter's (1971) concept of integration which he termed as

> . . . the process of transferring exclusive expectations of benefits from the nation-state to some larger entity. It encompasses the process by virtue of which national actors of all sorts (government officials, interest group spokesmen, politicians as well as ordinary people) cease to identify themselves and their future welfare entirely with their own national government and its policies (Schmitter, in Lindberg and Schmitter, 1971; p 238).

Sweeny (1984) underpins the theoretical aspect of the EU with functionalism and defines it in terms of the distinction between the general will and the will of all. For functionalists, the general will resides with those concerned with the non-political welfare needs of all people. Webb (1983) considered that European integration had produced a policy-making system that was partially integrated, but that political integration was unlikely and neo-functionalism was obsolete. She suggested that only two realistic frameworks remained:

intergovernmentalism and interdependence[5]. However, there are a number of different interpretations of interdependence (Rosecrance *et al*, 1977; Keohane and Nye, 1977; Cooper, 1977; Taylor 1980). The main problem with the theory is ". . . that it tends to ignore the relationship between *Gemeinschaft* and *Gesselschaft* that is found in any political process. The form which this relationship usually takes is the modification of perceptions of self-interest by such factors as emotional ties, preferences 'we feeling' or the identification of mutual values" (Taylor, 1980; p 373). This thesis questions the extent to which there has, or has not been, a shift in the EU from a pure *Gemeinschaft* toward the *Gessellschaft* (a shift from interdependence ground in intergovernmentalism toward integration through neo-functionalism).

> In other words, the realisation that interests are mutual is expected to precede the procedural or constitutional arrangements, and interdependence is seen to involve a learning process by which decision-makers are brought to recognise common interests (ibid).

Haas (1976) also identifies such a process in his concept of turbulence where clashing perceptions create confusion and ". . . everything is up for grabs" (p 179). The complexity of the situation is not based on limited knowledge but on too much, ". . . turbulent fields are the existence of very large bodies of knowledge . . ." which ". . . provide certainty for parts . . ." but confuse the whole (ibid). Garrett (1992) considers the difficulties of co-operation and the problems of discriminating between outcomes but when he spoke of preferences he spoke of government preferences. Indeed, there was little

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[5] Keohane and Nye (1977) examined the basic principles of interdependence and considered that in general terms the theory accepted the *Gessellschaft* theory of society rather than the *Gemeinschaft*. The former stresses the management of the market place in which conficting interests interact. The latter concentrates on consensus, stability and duty. It emphasises relationships between actors and considers that interests may be modified in respect of mutuality and preferred relationships.

mention of interest groups. However, Garrett and Weingast (1993) indicate how interest groups provide the basis for shared beliefs and "focal points" (p 176) which assists in the creation of certainty and understanding, the outcome of which, is further integration. This area is also explored in Haas (1975) where knowledge and space are again questioned in relation to integration, as it is by Derrida (1992) with regard to the concept of Europe. What are the boundaries of Europe? What is Europe? Is it no more than a peninsula of Asia? Additionally, Graubard (1963) posits the need for a new Europe. He questions the first forty years of the twentieth century, the concept of nationalism and concedes the demise of both the socialist and liberal utopias. He considered that Europe should be optimistic and that ". . . the present efforts, seemingly chaotic, may in time be viewed as the uncertain strivings of an old society to renew itself, by taking what is best from its recollections of a not undistinguished past" (p 653).

More recently, an interpretation of neo-functionalism has been proposed by Keohane and Hoffman (1990) who consider a more complicated understanding of 'spillover' between domains and sectors[6]. They contend that successful spillover necessitates prior agreements among Member States in terms of the SEA and the Maastricht Treaty etc. This thesis considers that such is necessary and that the spillover process, in Wallace's (1991, pp 8-12) terms, the formal aspect of integration, or the intergovernmental process, is forced through the informal or the neo-functional process. This necessitates further formal integration, or further treaties. Consequently, an extension of the treaties, e.g. the SEA and the Maastricht Treaty, creates an impetus for the informal, neo-functional process which through spillover puts further pressure on the formal (see Chapter Eight).

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[6] The difference between domains and sectors could be percieved as the diference between intergovernmental spillover (domain) and neo-functional spillover (sector). This thesis takes this idea further by considering different forms of neo-functional spillover.

Mutimer (1989) revisits neo-functionalism and emphasises the importance of the SEA. He also considers that federalism is inappropriate when analysing the EU. However, he eventually dismisses neo-functionalism because ". . . even in amended form it is not sufficient" (ibid p 101); this, one may consider, is rather an ambitious statement given the evidence that his paper provides. Pederson (1992) considers that intergovernmentalism should be combined with elements of neo-functionalism to enable a new framework of analysis. Keohane and Hoffman (1990, 1991) emphasise a pooling of sovereignty rather than its transference from the Member States to supranational institutions. A stronger intergovernmental stance is taken by Moravcsik (1991, 1993) whose analysis of the SEA considers that the primary source of integration resides with the Member States themselves. A more neo-functional perspective is taken by Sandholtz and Zysman (1989) who contended that three groups reshaped the EU: industrial elites, EU institutions and Member State governments. Furthermore, Sandholtz (1994) investigates why Member States are prepared to give up their currencies and the sovereignty this entails. He contends that membership of the EU defines preference parameters and decisions. Intergovernmentalism alone fails to explain the impact that membership of the EU has on Member State preferences, interests and demands. Indeed, if European integration is to be fully understood a combination of approaches is necessary. This is a theme that has also been posited by Tranholme-Mikkelsen (1991), George (1994, 1995), Garrett and Tsebelis (1996), Gehring (1996), Richardson (1996a), Ugur (1997) who also consider that further empirical work is necessary to enable greater understanding.

In an empirical study of European integration over the late 1960s and early 1970s, Kirchner (1976) argues that the ". . . logic and forces outlined by Haas

were generally found to be operative" (p 4). However, in a later work he contends that neither neo-functionalism nor intergovernmentalism adequately capture ". . . the existing overlap in decision-making between national and Community authorities, the sharing of joint tasks and interests, and the fusion of competencies between the national and Community level" (Kirchner, 1992; p 35). Pierson (1996) relies on neo-functional criticisms of intergovernmentalism and posits historical institutionalism as a means of understanding European integration[7]. Furthermore, Corbey (1995) amends neo-functionalism and argues that dialectical functionalism provides the impetus for European integration. Indeed, neo-functionalism considers that integration is ". . . a process of action (decision to act) and reaction (response to integration). Progress is generated by the mutual interaction of the institutions of the EU, member states, and interest groups, Since integration proceeds in stages, the dialectics of the process has to be given more attention" (pp 262-63).

Peterson (1995) considers that ". . . the gap remains wide between theoretical models which seek to explain broad patterns of European integration and those which seek to explain the EU's policy-making process" (p 69) However, the debate has turned toward governance through the arguments initiated by Keohane and Hoffman (1991), Marks (1993) and Marks *et al* (1996; 1996a). A number of questions have been formed regarding the political order that is emerging in the EU and based on more general theories, policy-making has been investigated. Indeed, two theories predominate within the debate.

> On the one side, functionalists and neo-functionalists have conceived of the process of institutional innovation as one of

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[7] Historical institutionalism is historical because things develop over time and institutional because this temporality is based in organisations through rules, structures and norms. Changes over time through changes in institutions or ". . . social processes understood as historical phenomenon" (Piersom, 1996; p 131).

integration in which supranational institutions compromise state autonomy and sovereignty by shaping institutional competencies, resources and decision-making rules. On the other side . . . intergovernmental theorists have argued that member states and their executives continue to dominate decision-making in the European Community . . . While they differ substantively, these contending accounts share a fundamental assumption about how to conceptualise the European Community. Both view the defining features of the outcome in terms of the relative role of supranational versus national institutions. They share a conception of the outcome of institution building in the European Community as varying along a dimension characterised by intergovernmentalism at one extreme and a supranational state at the other (Marks, 1993; p 391).

Hooghe and Marks (1997) link neo-functionalism (through supranational actors and interest groups) to multi-level governance and intergovernmentalism to state-centric governance. They conclude that the state-centric approach is not capable of fully explaining European policy making processes; that EU decision-making and policy-making are of a multi-level nature. Indeed, Marks *et al* (1996) provide an interesting interpretation of the present situation. "Multi-level governance does not confront the sovereignty of states directly. Instead of being explicitly challenged states in the European Union are being melded gently into multi-level polity by their leaders and the actions of numerous sub-national and supranational actors. State-centric theorists are right when they argue that states are extremely powerful institutions that are capable of crushing direct threats to their existence" (p 371). However, it is not necessary ". . . to argue that states are on

the verge of political extinction to believe that their control of those living in their territories has significantly weakened" (ibid). (For a critical overview of European integration theories and the current state of the debate, see Cram, 1997).

Interest group studies have been undertaken in an attempt to allow further understanding of European integration. The growth in the validity of the EU as a decision-making entity is made evident by the proliferation of interest group activity in aftermath of the SEA (Mazey and Richardson, 1992; 1993; 1996). Involved in the overview of the theories is the neo-pluralist and neo-corporatist schools (Schmitter, 1990; Streeck, 1989; Grant, 1990; Streeck and Schmitter, 1991; and Jordan 1991). There is also a strong emphasis on pluralism in the EU (Grant, 1989; Kirchner and Schwaiger, 1981; Sargent, 1987). However, this thesis concentrates on intergovernmental and neo-functional processes.

A number of theorists concern themselves with interest groups in general (Sidjanski, 1970; Averyt, 1975). Kirchner (1980) provides an analysis of the formation and development of interest groups at the European level and gives an indication of the characteristics of the groups and their interaction with the European decision-making bodies. He also provides an illustration of the top twenty-one interest groups at the European level, indicating in general terms how they attempt to influence decision-making in Europe (ibid, p 111). In more general terms there has been some analysis of interest groups in relation to the European Union (Lieber, 1974; Mazey and Richardson, 1992; Grant, 1995) each considering that further empirical work was necessary. Sidjanski (1970) proposed that groups establish themselves at the European level because they recognise a new centre of decision-making. As the EU began to affect certain interests, organisations congregated around the new

institutions ". . . sometimes . . . prompted by invitation or even pressure from the Commission" (p 402). Following an empirical study of European decision-making processes Mazey and Richardson (1996) support the idea of interest group/Commission interaction and provide clear evidence that consultation and lobbying are prolific. Indeed, both Sidjanski and Mazey and Richardson support elements of a neo-functional process.

Further work has recently been done in terms of identifying precise interest groups and analysing the process at the European level in terms of the harmonisation of specific industries. However, much of this has concentrated on industrial goods and procurement from a neo-corporatist standpoint. (Greenwood *et al*, 1992; Greenwood, 1995; 1997; Maloney, 1993; McLaughlin *et al*, 1993; McLaughlin and Greenwood, 1995; McLaughlin, 1995). Some consider that interest groups at the EU level are far from the dynamic entities perceived by Haas (McLaughlin *et al*, 1993; Schneider *et al*, 1994). Greenwood and Cram (1996) point out that there ". . . have been cases where national associations have undermined the collective agreement of the European federation by going direct to the Commission" (p 460). Furthermore, in some instances, there is competition between national and European interest groups. Indeed, in certain sectors individual companies lobby the Commission directly. McLaughlin *et al* (1993) suggest that European interest groups are undermined by large companies entering the political system themselves. "However, collective action is shown to be an indispensable option for large companies lobbying in Europe" (p 191). Camerra-Rowe (1996) concludes that there are variations from sector to sector in patterns of interest group representation and analyses interest group potency in respect of the automobile and insurance sectors. Andersen and Eliassen (1991) offer a synopsis of the differences between financial sector and agriculture interest groups. Ultimately, they posit the need for further democratisation of

European institutions and point in the direction of the European Parliament. The insurance sector is considered to have a unified and influential interest group because companies are willing to accept interest group representation. Indeed, the Commission promotes interest group representation. However, it does prefer European-wide interest federations over representatives of individual or national organisations (OJ/93C 63/03). Furthermore, ". . . both the European Commission and the European Parliament frequently stress that they want to speak to European organisations" (Club De Bruxelles, 1994; p 96).

This thesis acknowledges these theoretical differentiation's, proposals and findings and wishes to provide further understanding of the issues. The above has overviewed the main aspects of the theoretical literature to provide an understanding of the discussions regarding neofunctionalism and intergovernmentalism. The main concern is to provide an understanding of the literature and point out how this thesis fits into the on-going debate regarding theoretical and practical processes of European integration.

This thesis concentrates on the life insurance industry which has a number of interest groups at both the national level [Association of British Insurers (ABI) in the UK] and European level [Comité Européen Des Assurance (CEA)] and [Bureau International Producteurs Assurances et Reassurances (BIPAR)] which is made up of smaller insurance companies and brokers. Through an analysis of this sector and the above interest groupings it attempts an understanding of European integration processes in theoretical and practical terms.

Life Insurance and Europe Union Literature

The Treaties of Rome state that the "liberalisation of . . . insurance services connected with the movements of capital shall be effected in step with the progressive liberalisation of capital" (Art 61 (2)) and that the ". . . movement of capital between Member States shall be freed from all restrictions by the end of the first stage at latest" (Art 67 (2)). If this is to be the case there are a number of areas to be taken into consideration in respect of Non-Tariff Barriers (NTBs). Through its concentration on the life insurance industry this thesis indicates the technical barriers in respect of legislated regulation that need harmonisation, if a SEM in life insurance is to be achieved.

In Chapter Five, an insurance regulation matrix is constructed through the information supplied by Lloyds (1991), Munich Re (1988), Sigma (1988-94) BIIC and CEA working papers, Pool (1991) and a survey of the EU insurance industry undertaken by the author. Carter and Greenway (1991), Dickinson (1990, 1994), Carter and Diacon (1991), and Ellis (1990, 1994, 1995) provide a general understanding of the insurance industry in Europe. Vipond (1995) outlines a view of insurance representation at the EU level and indicates how national positions are compromised in the European interest group CEA. Cecchini (1988) gives an analysis of the benefits to be gained from the single market and the extent to which insurance is an important aspect of this. A political emphasis is illustrated in the Commission White Paper (1985), the Treaties (1988), the Maastricht Treaty (1991) and the Commission Report (1992). Randone (1990) and Canzano (1994) indicate that the way forward is in planning and creating a strategy for Europe and along with Jur *et al* (1989) acknowledge the need for legislation that facilitates cross-border trade.

Pool (1992) illustrates the link between the evolution of the Union, its growing membership, its institutions and the progression of its legal framework. He describes how the Commission and the Treaties are part of the decision-making process but he does not indicate whether or not the insurance industry has a part to play in this process; the CEA contends that it does and that as an interest group, it is central to the process.

Considering that diverse life insurance legislation existed throughout the EU, how was an SEM in life insurance to be achieved? Eltis and Spencer (1993) acknowledge this problem and consider mutual recognition and the co-ordination of essential minimum levels of supervision and co-operation between supervisors to be the way forward. Loheac (1992) considers that the third generation of insurance directives constituted a "cultural revolution" which affected all European financial sectors and that the operation of insurance would not be left unaffected by legal developments in the EU. Indeed, all Member State industries would be affected in some way by the changes in legislation and, as integration grew, differing legislative norms would become more apparent and the more difficult it would become to meet minimum conditions to overcome this diversity (Loheac 1991). In the latter work Loheac identifies regional grouping through integration and a convergence of regulation that he hopes will create further trading between Member States.

Corley (1992) considered that the Third Life Assurance Directive would allow a SEM in life insurance, at least as far as supervision was concerned[8]. However, he contended that there were differences in the attitude to risk between Member States, which were not a result of regulation or economic

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[8] The Third Life Assurance Directive is the latest legislation regarding cross-border trade for life insurance in the SEM. It allows home supervision and a licence to trade anywhere in the EU. It it defined further below (Chapter Eight).

development. Heseltine (1992) looked toward greater harmonisation in the SEM and proposed further consultation with business and welcomed constructive dialogue between the insurance industry and government stating that this was ". . . an absolutely essential foundation" (p 5) as were the close relations between the insurance industry and the Department of Trade and Industry (DTI). Heseltine considered that ". . . less legislation is the UK way" (ibid) and contended that he wished to persuade the rest of the EU of this. However, he did take into account the special nature of insurance and the need for a modicum of regulation.

Palliser (1992) contends that the insurance sector has been shaped by legislation and ". . . that in time the harmonisation of regulatory frameworks should introduce open competition in the life insurance market across the Community" (p 4). Additionally, Majone (1990; 1996) Mayer (1995), McGowan and Seabright (1995) and Ogus (1993) provide an overview of regulation in general and how it has evolved especially in respect of the EU.

Further work on the insurance industry in Europe has been undertaken by Drabbe (1994) and Canzano (1994) who investigated whether a single market in insurance is a realistic goal. Boleat (1995) considered whether a single market in insurance had been realised: the answer to which was "no". The potential of the market is discussed by Fitchew (1990), who indicated that the changes would not happen immediately and realised as early as 1990 that the completion of an internal market in insurance would not be completed by 1993 but only be in its infancy. Frangoulis (1988) considered that there would be little change especially over the first four or five years. He thought that the industry would need time to acclimatise to the changes. This was reinforced by O'Leary (1988) but he contended that eventually the single market would be realised and the UK should ready itself for this occurrence. Russell (1988)

admitted that harmonisation was likely to happen and that two areas should be concentrated on with regard to regulation: protection and market opportunities.

This thesis illustrates how the SEM is evolving and indicates how this may be part of integration processes that are creating further European union: that the Treaties force the process and through *self-interest* and *mutual assistance* industries and sectors are proactive in the formation of the SEM and this necessitates extensions of the Treaties and further integration. European information can primarily be found in the Official Journals Commission and Parliamentary publications. The interest group compromises can be perceived in CEA, BIIC and ABI briefing papers.

Included in the process of integration is the free movement of services and this is where the need to harmonise the insurance industry springs from. Cecchini (1986) identified the losses that Europe incurs because of the NTBs that Member States create; this gave an economic impetus to union whereas the treaties exemplified the political will. This provides a means by which one may identify both intergovernmental and neo-functional processes in the creation of regulatory conditions. The life insurance market is an important area in the completion of the SEM. However, agreement in this sector is invariably difficult to attain. This study provides an empirical account of the decision-making processes regarding the Third Life Assurance Directive and the attempt to create a single market in life insurance and an analysis of the theoretical propositions that this empirical account creates.

Conclusion

It has been necessary to break the literature review down into three parts: Methodology, Post-War Integration Theory and Life Insurance and European Union. This has been done to illustrate the extent of the literature used in the thesis and how each part relates to the other. Functionalism, neo-functionalism and interest groups are related because the theories rely heavily on interest group usage; this is especially so of neo-functionalism. Each part of the theoretical literature concludes that there is a necessity for empirical studies and considers that European integration should be reassessed through these empirical studies.

This thesis revisits and reassesses European integration from both theoretical and empirical perspectives. The methodology has attempted to understand neo-functionalism and intergovernmentalism from a grounded theory perspective. Grounded theory considers that theories are not proved or disproved but added to or detracted from. Theory is an on-going and an interaction between inductive and deductive processes. Through grounded theory methodology, some of the criticisms levelled at neo-functionalism may be overcome, especially with respect to the absence of a dependent variable. On an empirical level an analysis of the decision-making processes regarding the European life industry allows a better understanding of neo-functional and intergovernmental processes. The literature indicates the debates and channels of influence that were at work in the creation of the single market in life insurance and signalled the direction that the empirical study should take in the creation of a substantive theory. Basically, the three areas provide the means by which a better understanding of the European integration process may be achieved and indicate levels of understanding that have been managed to date. The next chapter introduces the methodology of

grounded theory and illustrates the data collection processes and interpretations that are the bases of the substantive theory.

Chapter Two

Methodology: A Grounded Theory Approach

> *Induction introduces us to first principles and universals, while deduction starts from universals. Therefore there are principles from which deduction starts which are not deducible; therefore they are reached by induction (Aristotle, 1983; p 207).*

Introduction

The main aim of this chapter is to illustrate how the thesis has applied grounded theory to European integration. To do this, the thesis, initially undertakes a comparative analysis and open coding of Member State life insurance legislation and through induction, deduction and verification formulates tables, matrices and models to illustrate harmonisation processes in the European decision-making process. Grounded theory wishes to construct substantive theory through coding data. Substantive theory necessitates four central criteria. *Fit, comprehension, generality and control*: the theory should be induced from diverse data and be faithful to reality (it should *fit*); secondly, the *fit* should be *comprehendable*; thirdly, the data should be comprehensive and interpretations conceptually wide (there should be *generality*); and finally, in relation to generality, it should be made clear when conditions apply to specific situations and phenomena (there should be *control*) (Corbin and Strauss, 1990). Indeed, hypothesis proposing relationships among concepts should be ground from the data. This chapter explains how the thesis constructs a substantive theory and illustrates the

extent to which it (the substantive theory) relates to pre-existing formal theories.

Substantive theory emerges from the analysis of a ". . . particular situational context", whereas formal theory ". . . emerges from a study of phenomenon under many different types of situations" (Corbin and Strauss, 1990; p 174). However, it is recognised that theories are never completed but always in the process of construction.

The Philosophical Roots of Grounded Theory

The Discovery of Grounded Theory (1967) ". . . provided a strong intellectual rationale for using qualitative research to develop theoretical analysis" (Charmaz, 1983; p 109). The approach provides the qualitative research area with a defined structure to enhance its credibility. Effectively, it was a demonstration against the predominance of quantitative research. Glaser and Strauss (1967) draw on Dewey (1950) Mead (1962) Blumer (1969) and the pragmatist tradition. Dewey considered that, ". . . flowers can be enjoyed without knowing about the interactions of soil, air, moisture and seeds of which they are the result. But they cannot be understood without taking just these interactions into account and theory is a matter of understanding" (Dewey, 1950; p 12). Theory cannot answer questions ". . . unless we are willing to find the germs and roots in matters of experience" (ibid). In the acquisition of knowledge, an essential element ". . . is the perception of relations, especially the relations between our actions and their empirical consequences." (Scheffler 1974 p 197). By this means, the world around us and we as individuals take on deeper meaning; in this context, humans need experience and the means of storing that experience. However, experience is more than ". . . a passive registering or beholding of phenomena; it involves

deliberate interaction with environmental conditions, the consequences of which are critically noted and fed back into the control of future conduct" (ibid).

Dewey, considered that from

> . . . the child's exploration of its environment to the scientist's theorising about nature the pattern of intelligent thought is the same: a problem provides the initial occasion of inquiry. Action is blocked, conflicts or difficulties create an unsettled situation. Deliberation is blocked; action turned inward; the resultant elaboration and competition of hypothetical ideas sparks action once more. Such action tests the idea that initiated it, for if the action settles the initial difficulty, the idea has worked in reorganising conduct in a more effective pattern . . . Experiment for Dewey is, experience rendered educative (ibid, p 196).

Indeed, grounded theory can be based on *symbolic interaction* (Mead, 1962) where the ". . . individual enters as such into his own experience only as an object not as a subject; and he can enter as an object only on the basis of social relations and interactions" (p 225). Through the language and structure of roles we become a generalised other; we attain a consciousness of self as a generalised other. This may allow the individual to take an impartial and general standpoint in observing and evaluating one's own conduct when one becomes a generalised other or the object of one's own reflection. At this point one has become self.

> One now regularly takes an impartial and general standpoint in observing and evaluating one's own conduct . . . (however) . . .

> The organised community or social group which gives to the individual his unity of self may be called the generalised other and is the attitude of the whole community (Blau, 1952; pp 162-163 author's brackets).

Blumer (1962; 1969) builds on the work of the pragmatist tradition and considered that, ". . . ordinarily human beings respond to one another, as in carrying on a conversation, by interpreting one anothers' actions or remarks and then reacting on the basis of interpretation" (Blumer, 1969; p 71). Grounded theory builds on this understanding and considers that the research should be grounded out of reality and that the researcher should get out into the field and discover/comprehend what is going on. People have an active role in shaping the world and through interrelationships in terms of meaning, action and conditions the nature of experience continually evolves (this creates changes in understanding phenomenon) (Corbin and Strauss, 1990). Indeed, grounded theory is primarily inductive and pursues the interpretations of those involved in the situation that is being researched and the interpretations of the researcher in relation to the data. Through this process grounded theory is pursued and substantive theory constructed.

Grounded Theory as Methodology

Grounded theory looks to the generation of theory through comparative analysis and does not attempt to undermine theory but better it. Indeed, ". . . a theory's only replacement is a better theory" (Glaser and Strauss, 1967; p 28). "Grounded theory is based on the systematic generation of theory from data, and itself is systematically obtained from social research. Thus, the grounded theory method offers a rigorous orderly guide to theory development that at each stage is closely integrated with a methodology of social research" (Glaser,

1978; p 2). Through the general method of comparative analysis, grounded theory wishes to create a theory made up of general categories. It is not necessary to know the concrete situation better than those involved in it. The analyst simply wishes to develop theory that applies to relevant behaviour. Theory is never a finished product, but always in the process of development. Generating a theory from data means that most of the ideas or hypotheses are not only derived from the data but are worked out in relation to the data as the research progresses.

While logico-deductive theory seeks to verify deduced hypotheses, grounded theory suggests that there should be a change of emphasis in respect of research methods and aims to emphasise the prior step of discovering what concepts and hypotheses are relevant to the area under research. Ultimately, the relationship between categories and sub-categories which are discovered during the research should be as a result of information contained within the data only, or from deductive reasoning which has been verified within the data, but not from previous assumptions which have not been supported (Cottingham and Hussey, 1996).

Research should be approached with an open mind and as much objectivity and distance as is possible. However, it is acknowledged that such objectivity is difficult, as everyone is instilled with subjective tendencies; yet recognising subjectivity is part way to overcoming it. This may be considered to encompass theoretical sensitivity which is initially gained by entering the research ". . . with as few predetermined ideas as possible especially logically deduced, a priori hypotheses" (Glaser, 1978; p 3). Such enables the researcher to remain sensitive and ". . . record events and detect happenings without first having them filtered through and squared with pre-existing hypotheses and biases" (ibid). However, there is a problem here: each of us has

predetermined ideas as each of us has different levels of sensitivity which depend on

> . . . previous reading and experience with or relevant to the area. . . . Theoretical sensitivity refers to the attribute of having insight, the ability to give meaning to data, the capacity to understand, and the capability to separate the pertinent from that which isn't. . . . It is theoretical sensitivity that allows one to develop a theory that is grounded conceptually dense (Strauss and Corbin, 1990; pp 41-40).

In a later publication, Glaser expanded on his earlier definition.

> Theoretical sensitivity refers to the researcher's knowledge, understanding, and skill which foster his generation of categories and properties and increase his ability to relate them into hypotheses, and to further integrate the hypotheses, according to emergent theoretical codes. Accomplishing this result in relevance, fit and work are the criteria of grounded theory (Glaser, 1992; p 27).

Grounded theory suggests that there is an over-emphasis on verification theory and wishes to demote the idea that the discovery of relevant concepts and hypotheses are *a priori* to research (Glaser and Strauss, 1967; Glaser, 1978; Charmaz, 1983; Strauss, 1987; Strauss and Corbin, 1990; Corbin and Strauss, 1990; Glaser, 1992; Strauss and Corbin, 1994). Grounded theory posits that theory is derived from data and consequentially illustrated through characteristic examples of data. Theory cannot be divorced from the process by which it is developed. Subsequently, most hypotheses and concepts are

generated through the data and worked out in relation to the data during the course of the research (Glaser and Strauss, 1967).

Initially, grounded theory is inductively derived from the study of the phenomena it represents. Data collection, analysis and theory are reciprocal with each other; one does not start with a theory which is then tested but an area of study from which what is relevant to the area becomes apparent. Induction needs to be grounded in social phenomena or observations and experience; hence the link between inductive and grounded theory (ibid).

Charmaz (1983) reiterates Glaser and Strauss (1967) when she contends that data collection and analysis are undertaken simultaneously and that interpretation is formed through data discovery and vice-versa. The approach allows for emerging ideas because it provides for further data collection. It accepts that one of the main strengths of the grounded theory approach is one where data and ideas are derived through the research rather than through *a priorism*. Verification is secondary to understanding processes, not simply the processes of the phenomenon, but the understanding that social life itself is a process.

> As such, theoretical analyses may be transcended by further work either by the original or later theorists. In keeping with their foundations in pragmatism, then, grounded theorists aim to develop fresh theoretical interpretations of the data rather than explicitly aim for any final or complete interpretation of it . . . Although every researcher brings to his or her research general preconceptions founded in expertise, theory, method, and experience, using the grounded theory method necessitates that

> the researcher look at the data from as many vantage points as possible (Charmaz, 1983; pp 111-114).

Data should be analysed as it emerges and through coding, "order created" (ibid).

This thesis acknowledges that it is easy to find a problem with a theoretical concept by identifying that certain data is missing. This could be the charge against most analyses. However, as Glaser and Strauss put it: "If each debunker thought about the potential value of comparative analysis . . . he would realise that he has merely posed another comparative datum for generating another theoretical property or category" (Glaser and Strauss, 1967; p 22). Despite what those concerned with evidence may say, nothing has been disproved, only another comparison created (ibid).

In general terms ". . . analysis makes use of constant comparisons. As incidents are noted, they should be continually compared against other incidents for dissimilarities and likenesses" (Corbin and Strauss, 1990; p 9). Initially, a comparison of EU Member State life insurance legislation was undertaken and the extent to which this legislation allowed trading freedom in the national life insurance market identified (Oyen, 1990). A study of the European life insurance industry was undertaken and a convergence of Member State legislation asserted. The initial research relies on a comparative study of legislation and links this to national differences. This is a standard means of generating theory and is usually accomplished early in the study to put the "story straight" (Glaser and Strauss, 1967; Strauss and Corbin, 1990; pp 116-142). "Making comparisons assists the researcher in guarding against bias .

. . comparisons also help to achieve greater precision (the grouping of like and only like phenomenon)" (Corbin and Strauss, 1990; p 9). Fundamentally, one is seeking regularities and this also creates order and helps with data integration.

Theoretical Coding

Theoretical coding is the basis of grounded theory. The essential relationship between data and theory is a conceptual code. The code conceptualises the underlying patterns of the data. "Thus, in generating a theory by developing the hypothetical relationships between conceptual codes (categories and their properties) which have been generated from the data as indicators, we discover a grounded theory" (Glaser, 1978; p 55).

Coding illustrates ". . . the fundamental analytical process used by the researcher" (Corbin and Strauss, 1990; p 9). Charmaz (1983) considers that coding incorporates ". . . the initial phase of the analytical method (and) is simply the process of categorising and sorting data. Codes then serve as shorthand devices to label, separate, compile and organise data. Codes range from simple concrete, and topical categories to more general, abstract conceptual categories for an emerging theory" (Charmaz, 1983; p 111). However, ". . . in grounded theory research there are three basic types of coding; open, axial and selective" (Corbin and Strauss, 1990; p 9).

Open coding examines phenomena through comparing and categorising data, whereas axial coding is the re-structuring of the whole process by finding connections between the data. Selective coding illustrates how the phenomenon fits around a core category (in this context, the existence of the EU and the SEM). Such leads on to 'process' whereby changes in the data are

monitored and made explicit. As noted above, grounded theory is both inductive and deductive, the deductive nature coming into play primarily in the pursuit of process. "As you have probably noticed while coding we are constantly moving between inductive and deductive thinking" (Strauss and Corbin, 1990; p 111). When process is difficult to identify, the researcher may turn to deductive analysis so as to identify, possible situations of change, ". . . then go back to the data or field situation and look for evidence to support refute or modify that hypothesis" (Strauss and Corbin, 1990; p 148).

Open Coding

"The goal of the analyst is to generate an emergent set of categories and their properties which fit, work and are relevant for integrating theory. To achieve this goal the analyst begins with open coding" (Glaser, 1978; p 56). Attention should be fixed on a category and the properties that emerge continually coded and analysed: these are the initial basic steps. Ultimately, one constantly compares and continually categorises.

"The grounded theory approach is a qualitative research method that uses a set of procedures to develop an inductively derived theory about a given phenomenon" (Corbin and Strauss, 1990; p 24). These procedures are coding techniques which, for this study, initially encompass a comparative analysis of the EU life insurance industry and the different regulatory systems of the separate Member States. The qualitative data on each regulatory environment is broken down in terms of open coding and restructured initially on a table and later refined in a matrix. The *category* of 'Regulatory Environment' emerged following an analysis of Member State legislation and regulations. Through further research *conceptual labels* emerged in terms of liberal, prescribed and state-controlled regulatory environments and each of these

was made up of the *properties* outlined in Table 2.1 (p 43). A *category* is a ". . . classification of concepts. This classification is discovered when concepts are compared one against another and appear to pertain to a similar phenomenon" (Corbin and Strauss, 1990; p 61). Furthermore, *conceptual labels* are placed ". . . on discrete happenings, events, and other instances of phenomena" (ibid). Indeed, these concepts are made up of *properties* and *characteristics* that are indicated by the overall category. Finally, the Member States are given *dimensions* through the ". . . location of properties along a continuum" (ibid), in this thesis a regulation matrix (see Life Insurance Regulation Matrix One, Fig 5.1 p 157). This process was pursued through the use of *code, theoretical, operational notes* and *diagrams; code notes* illustrate separate types of legislation in the different Member States and how aspects of the legislation link together and fluctuate under *conceptual labels; theoretical notes* link different types of cultural existence to the conceptual labels and questions how compromises take place. Through the *operational notes* the need for further research is illustrated. The *operational notes* guided the research in respect of: who to survey; the questions to be asked; and further into the research, who should be interviewed and the structure the interviews should take. Overall, the research was visually represented through *diagrams* each of which illustrated the relationship between concepts. Indeed, the *diagrams* illustrate a ". . . visual sorting process that helps you identify how the categories are related to one another" (ibid p 197).

In practical terms, the open coding process was used to create a scale of one to twelve on which a totally liberal regulatory environment is valued at one and a completely state-controlled or nationalised regulatory environment is valued at twelve. A prescribed regulatory environment is considered not to be one of primarily self-regulation, nor is it state-controlled: it is a market

Table 2.1
Regulatory/ Legislative Environment Table
(CATEGORY)

Regulatory Environments	Legislative/Regulatory Stipulations	Member States
Liberal (CONCEPTUAL LABEL)	**(PROPERTIES)**	**(DIMENSIONAL-ISATION)**
1	Completely free market	
	Approval of Company	
2 - 3	Solvency Margins	Luxembourg
	Policyholder protection	
	Evaluation of Liability	Netherlands
	& Rates	UK
3 - 4	Open Access to Insurance	
	Information	Eire
Prescribed		
5 - 6	Price Controls	Belgium
	Marketing Controls	Denmark
	Solvency Deposit	Spain
7 - 8	Policy Approval	
	Regulation of Contract	Germany
State-Controlled		
9 - 10	State Controlled Companies	France
	Contractual Obligation to	
	State	Italy
10 - 11	Intense Monitoring of	
	Companies	Portugal
	Proof of Ability	Greece
12	Total State Control	

with tight government regulations (see the Regulatory/Legislative Environment Table 2.1 p 43 and the Data Collection Scheme, Table 2.2 p 50).

The higher the number on the table, the greater the regulation and state-control indicated in the Member State's legislative system. Through further comparative analysis and open coding each Member State was understood to be at some point on a matrix scale (see Life Insurance Regulation Matrix One, Fig 5.1 p 157).

Once this had been accomplished, it was felt that some further investigation was necessary and a survey of the European life insurance sector was undertaken (see Data Collection Scheme, Table 2.2, and survey A, Appendix A, p 330). The matrix was subsequently revised taking into consideration the survey results which also raised further questions (Life Insurance Regulation Matrix Two, Fig 5.2, p 160). Ultimately, a secondary analysis was made of the data and further coding generated. In summary, through an analysis of each national market's legislation, a regulation matrix was created which could be verified and further analysed through a survey. The survey then added data to the regulation matrix and a greater understanding of the European life insurance industry regulatory structure was generated.

Axial Coding

Axial coding involves bringing the analysis together, to create a whole. It indicates the overall system of which the categories created through open coding are part. In this thesis, axial coding is verified through the interviews and further explained by the subsequent European Decision-Making Model (see Chapter Seven) It is inclusive of:

(a) Causal conditions.

(b) Phenomenon.

(c) Context.

(d) Intervening conditions.

(e) Action/Interaction.

(f) Consequences.

(Corbin and Strauss, 1990; pp 96-97).

An application of axial coding in this thesis is identified through:

(a) Membership of the EU.

(b) The creation of the SEM and legislation to create regulatory environments.

(c) The European decision-making process.

(d) The harmonisation of different Member State concepts of market conditions (life insurance industries).

(e) Interaction between Member States and decision-making bodies.

(i) Goal orientation (purposeful) market as near to one's own. Interaction between Member states at the European interest group level.

(ii) Evolutionary changes (processional) compromised issues. Interaction between interest groups and the EU decision-making institutions.

(f) Outcomes or the creation of a harmonised SEM in the life insurance sector; a move towards greater European integration.

In more specific terms, the *causal conditions* and *phenomenon* are membership of the EU and the on going evolution of the SEM. The *context* is the possible shift in sovereignty in terms of the decision-making process and market control. The *intervening conditions* are the necessities of harmonisation and the implications this has for integration; such is

illustrated through the compromises made by Member States in respect of regulatory environments. It portrays the need for *action/interaction* between Member States and the European decision-making institutions in terms of the evolutionary changes taking place i.e. the need to harmonise and create a SEM and the goal oriented interaction of creating legislation as close to one's own as possible. Finally, the *consequences* are the creation of the SEM through harmonisation and a shift toward greater European integration and closer European union.

Glaser considers that axial coding ". . . undermines and confuses the very method that he (Strauss) is trying to build" (Glaser, 1992; p 61). This process forces the data and negates theoretical coding. The grounded theorist should code categories and properties and allow theoretical codes to emerge where they will. Strauss and Corbin consider that axial coding allows a more focused means of discovering and relating categories.

> That is, we develop each category (phenomenon) in terms of causal conditions that give rise to it, the specific dimensional location of this phenomenon in terms of its properties, the context, the action/interaction strategies used to handle, manage, respond to this phenomenon in light of that context, and the consequences of any action/interaction that is taken. Furthermore, in axial coding we continue to look for additional properties of each category, and to note the dimensional location of each incident, happening or event (Strauss and Corbin, 1990; pp 114-115).

This research uses Corbin and Strauss' axial coding as a guide into which emerge the specific categories to the study i.e. those categories outlined above.

Selective Coding

"Selective coding is the process by which all categories are unified around a core category" (Corbin and Strauss, 1990; p 15). The core category in this study is the European Union and the process of European integration. The SEM in life insurance and regulatory environments incorporate ". . . other categories and stand in relationship to the core category as conditions, action/interactional strategies, or consequences" (ibid). The selection of data and the creation of other categories have been processed with the core category in mind. "The core category represents the central phenomenon of the study. It is identified by asking questions such as; what is the main analytical idea presented in this research? What does all the action/interaction seem to be about?" (ibid). The answers to which are: the integration processes at work in the EU, how Member States' action/interaction create the SEM and how this adds impetus to European integration. These areas are identified and unified through axial coding. "During axial coding, one begins to notice certain patterns . . . and a certain amount of integration naturally occurs" (ibid p 130). Indeed, a network of conceptual relationships already exists. Of course, the network may be unclear but these can be refined during selective coding. "It is very important to identify these patterns and to group the data accordingly, because this is what gives the theory specificity" (ibid). To clarify connections in the network grounded theory uses " . . . a combination of inductive and deductive thinking, in which we move between asking questions, generating hypotheses, and making comparisons" (ibid, p 131). Selective coding integrates the research, it puts the story straight, provides analysis, identifies the core category and illustrates how major categories relate, both to it and to each other. This can be further developed through understanding *process*.

Process: Self-Interest & Social Mutuality

Process is also be built into the theory. "Process analysis can mean breaking a phenomenon down into stages, phases, or steps. Process may also denote purposeful action/interaction that is not necessarily progressive, but changes in response to prevailing conditions" (Corbin and Strauss, 1990; p 10). Consequently, when the life insurance sector and EU decision-making institutions are analysed, processes and action/interaction are identified through interest groups. The changes and compromises made by interest groups and sectors are interpreted in relation to the changes the SEM has brought and is bringing about.

The analysis identified process in the Member State markets because of their membership of the EU and the creation of a piece of legislation that would harmonise the different market environments. This would create the need for compromises; and the research sought to identify why and how these compromises and changes would take place. Consequently, a model was constructed through semi-formal interviews, participatory observation and the third survey (survey C, see Data Collection Scheme, Table 2.2, p 50 and Appendix A, p 330). Each of the surveys assisted in theory generation; the results of survey A (see Data Collection Scheme, Table 2.2, Appendix A and pp 158-68, for results) describe the processes at work which lead to theory generation and are used as secondary analysis with regard to the comparative analysis of Member State insurance industries. "Comparative analysis requires secondary analysis when populations from several different studies are compared, such as different nations or factories" (Glaser and Strauss, 1967; p 188). Surveys B and C are used in the same way with regard to the decision-making model (see Data Collection Scheme, Table 2.2, and Appendix A).

From an assumption of the maximisation of *self-interest*, the convergence of legislation is examined. However, the research does recognise the difficulties with indicating *self-interest* alone as a motivator and considers that an ethical/welfare stand-point is a factor (Sen 1992).

Through a compromise being reached at the European level, *self-interest* is sacrificed for the general good or welfare even though this is initially in a limited area[1]. However, ultimately welfare is realised throughout Europe in terms of peaceful co-existence and economic expansion. As Scheingold indicated ". . . integration was good by definition since it was directed at economic reconstruction and permanent reconciliation between nations whose conflicts had led to bloody wars . . . A 'United States of Europe' seemed almost by definition likely to serve the cause of a peaceful and prosperous future" (Scheingold, 1971; p 30).

The Data Collection Scheme.

The data collection part of the research (or the methods used) is a balance between interviews, participatory observation and surveys. Indeed sampling has been based on the grounded theory technique of *theoretical sampling*. *Theoretical sampling* is undertaken on the basis that ". . . concepts have *proven theoretical relevance* to the evolving theory"(Strauss and Corbin, 1990; p 176). *Proven theoretical relevance* identifies concepts that are significant enough to considered *categories* " . . . they are deemed significant because (1) they are repeatedly present or notably absent when comparing incident after incident (2) through coding procedures they earn the status of

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[1] Welfare in this thesis is based on the concept of the social contract, as in, the need for people to work and exist together so they are able to pursue their self interest. It is based on Kant's civic constitution, Durkheim's organic society and Rawl's veil of ignorance. It is giving up one's individual freedom in certain areas for the welfare or general good of all.

categories. . . . The aim of theoretical sampling is to sample events, incidents, and so forth, that are indicative of categories, their properties and dimensions, so that you can develop and conceptually relate them" (ibid, p 177). *Theoretical sampling* involves three processes: *open sampling* which relates to *open coding; relational and variational sampling* which is associated with *axial coding;* and *discriminate coding* which is linked to *selective coding.*

Table. 2.2
Data Collection Scheme

Survey A: Survey of European Union life insurance companies. Allows an understanding of market environment perceptions from separate Member States. *Open sampling* and *relational* and *variational sampling*

Survey B: Survey of European Parliament, Permanent Representatives, Member State insurance interest groups, Lobbyists and the Commission. This provides a picture of the parts played by organisations in the decision-making process. *Relational and variational sampling*

Survey C: Survey of UK insurance companies to ascertain interest group utilisation. *Discriminate coding*

Interviews: The interviews are supplemented by survey C and provide an in-depth understanding of the EU decision-making process with regard to the Third Life Assurance Directive. *Relational* and *variational sampling* and *discriminate coding*

Observations and preliminary discussions: This incorporated three months in Brussels working with a European political consultant (GJW), a period with the European section of a UK company (Commercial Union) open discussions and close contact with the Association of British Insurers (ABI). *Open sampling*

Following an inductive analysis of the different Member States' life insurance legislation and a survey (survey A, see Table 2.2 and Appendix A, p 330) of the European life insurance industry, a regulatory environment matrix was created. This part of the of the analysis illustrates *open sampling* where the

aim is ". . . to uncover as many potentially relevant categories as possible along with their properties and dimensions" (ibid, p 181) and the beginnings of *relational and variational sampling*. Indeed, the survey validates the relationships between the categories and identifies processes. From this some propositions were formed and the sampling gradually became specifically *relational and variational*. The sampling was undertaken purposefully. This encompassed choosing individuals and documentation that demonstrated variations in the categories and what happened when change occurred. Fundamentally, as with the coding process the distinction between *relational and variational sampling* and *discriminate sampling* became unclear. *Discriminate sampling* is direct and deliberate and is indicated by the choice of interviewees and survey C. "In discriminate sampling, a researcher chooses the sites, persons and documents that will maximise opportunities for verifying the story line, relationships between categories" (ibid, p 187). Sampling in grounded theory studies is concerned with the ". . . representativeness of concepts in their varying forms. In each instance of data collection, we look for evidence of its significant presence or absence, and ask why?" (ibid, p 190). Grounded theory studies look ". . . for incidents and events that are indicative of phenomena" (ibid). Indeed, they pursue density and ". . . the more interviews, observations and documents obtained, then the more evidence will accumulate, the more variations will be found, and the greater the density will be achieved. Thus there will be wider applicability of the theory, because more and different sets of conditions affecting phenomena are uncovered" (ibid pp 190-91).

This process subsequently set up a number of questions which were investigated through semi-formal interviews with key individuals in the creation of the Third Life Assurance Directive and through participatory observations of the European decision-making process. These gave an

understanding of the political process and enabled further construction of a theoretical model. Table 2.2 summarises the data collection process in terms of three surveys, the interviews and participatory observations. In survey A, three hundred questionnaires were sent to insurance companies in eight of twelve Member States, (the UK, Germany, France, Italy, Belgium, Netherlands, Spain and Eire). Four Member States were omitted mainly because of problems with translation and difficulties in terms of acquiring addresses. The response rate was 35-40% which are listed and analysed below in Chapter Five. The survey wished to illustrate the thoughts of the Member States with regard to national life insurance regulation and the creation of a single market. It also aimed to determine the extent of freedom allowed by the amount of regulation within a particular Member State and to illustrate what the respondents considered to be the optimum regulation for trading and the amount of legislation necessary to enable this.

A survey of the European life insurance industry was used instead of interviews, because a broad sample was required to add to the regulatory environment matrix which encompassed the industry's understanding of the SEM and the EU. Indeed, the survey provided an understanding of the differences in Member State normative thinking in respect of life insurance regulation and raised the question of where and how compromise takes place in the creation of the SEM.

Indeed, the questionnaire follows *self-interest rationality* in terms of competitive advantage in the evolving EU: however, at the same time it attempts to recognise other aspects of motivation in the process e.g. welfare. (Sen 1993).

One may consider that an environment free of regulation is an impossibility, and in a post-cold war situation, total state control untenable. This may be indicated by competition policy at the SEM level. It may be argued that no trading structure can exist without some form of regulation which invariably indicates legislation. What the survey wished to ascertain was the extent to which legislation has an effect on the regulatory environment within which a Member States' company traded and what type of regulatory environment would be most amenable to all Member States at the EU level.

In a second survey (survey B, see Table 2.2, and Appendix A), questionnaires were sent to interest groups, lobbyists and Permanent Representatives (Finance Committees). This survey was of a qualitative nature and was reinforced by interviews.

Finally, a third survey (survey C see Table 2.2 and Appendix A) of the UK insurance sector attempted to ascertain how companies approached the European and national legislatures. Respondents were asked to indicate the extent to which they agreed or disagreed with a series of statements using a likert scale: one=strongly agree; two=agree, three=disagree, four=strongly disagree. This survey was used to identify the extent to which interest groups were used in the process of legislation creation and looked to verify or question the idea that European interest groups are used in the process of EU decision-making.

The Role of Surveys in Grounded Theory

Within the grounded theory methodology, surveys and quantitative data play an ambiguous role. "The sociologist whose purpose is to generate theory may of course collect his own survey data, but, for several reasons, he is more

likely to analyse previously collected data-called secondary analysis" (Glaser and Strauss, 1987; p 187). However, the researcher should give him/herself the ". . . freedom in the flexible use of quantitative data or he or she will not be able to generate theory that is adequate. . . (and) in taking this freedom he must be clear about the rules he is relaxing (ibid, p 186). Indeed, such flexibility will allow the richness of qualitative data to become apparent ". . . and lead to new styles and strategies of quantitative analysis, with their own rules yet to be discovered . . . For example, in verification studies cross-tabulations of quantitative variables continually and inadvertently lead to discoveries of new social patterns and new hypotheses that are often ignored as not being the purpose of the research (ibid).

Basically, grounded theory wishes to relax the rules of verification and accuracy of evidence to enable further theory generation ". . . the way they are relaxed for purposes of generating theory could apply to many styles of analysis" (ibid, p 187). "One might use qualitative data to illustrate or clarify quantitatively derived findings; or, one could quantify demographic findings. Or, one could use some form of quantitative data to partially validate one's qualitative analysis" (Strauss and Corbin, 1990; pp 18-19). Such may be realised through triangulation. Indeed, as grounded theory itself is a theory it may never be completed (this would contradict grounded theory). Consequently, although surveys are not purely grounded theory techniques, used in certain ways they may benefit theory generation. In this context, they may be utilised in a grounded theory study and eventually they may be considered as part of the technique. This, one may speculate, is the direction in which Glaser and Strauss pointed in 1967. In 1992 Glaser makes this clear. "To repeat, qualitative analysis may be done with data arrived at quantitatively or qualitatively or in some combination" (Glaser, 1992; p 11). And how they may be used ". . . together effectively . . . depends on the research" (ibid, p 12).

The Interviews

Interviews were used to investigate decision-making processes at the European level. Over an eight week period working for a political lobbying company (GJW Political Consultants) in Brussels, the author was able to gain access to decision-makers. Interviews were undertaken with the Commission; insurance interest groups; the UK Permanent Representative (Finance Committee), and lobbyists. Further interviews were undertaken in Paris and the UK.

The interviews were 'moderately structured' (Carlson, 1984) and were based on a number of informal discussions with individuals from the UK insurance industry. In carrying out the interviews, the interviewer gave a brief outline of what was thought to be the process. Direct questions were then asked which allowed for further questions, further elaboration was pursued until little more could be ascertained. The direct questions asked were in the forms outlined in Appendix B.

Each interview attempted to look at the same phenomenon from a different perspective and enable data saturation and triangulation. The interviews were conducted between surveys B and C and indicated the need for survey C (see Table 2.2 and Appendix A p 300). The need for legislative convergence is indicated by the open coding process, the surveys and consequent matrix. Additionally, the interviews and survey C allow the construction of a model of EU decision making processes. Indeed, they illustrate verification and the processes of selective and axial coding. Subsequently, through the use of both the matrix and the model, a substantive theory is constructed that illustrates convergence and harmonisation procedures in the EU. Ultimately, a

substantive theory of European integration is illustrated that has aspects of both neo-functionalism and intergovernmentalism (formal theories).

Substantive Theory

The substantive theory is built through coding, categorisation and process. The matrices provide the basis of the substantive theory in that they acknowledge that separate Member States pursue different market regimes. This sets up the problem of understanding how compromise is reached. The interviews, participatory observations and survey C further construct the substantive theory with regard to the EU decision-making process. This substantive theory has implications for the formal theory of neo-functionalism in terms of spillover, supranationality and interest group utilisation.

"A substantive theory generated from the data must be formulated, in order to see which of diverse formal theories are, perhaps, applicable for furthering additional substantive formulations" (Glaser and Strauss, 1967; p 34). This illustrates that theories are never complete but processes in themselves. In this context, one may question the extent to which neo-functionalism may be labelled a formal theory, and question the extent to which it is a substantive theory of integration theory in that it has not really emerged from studies under different types of situations i.e. integration processes external to western Europe. Thus, one may question the extent to which neo-functionalism or intergovernmentalism may be labelled formal theories.

Formal Theory

> A formal theory is composed of a model plus an indefinite number of interpretations, and there is a sharp distinction between model and interpretation. A model is not affected by any of its interpretations, but can be understood and studied in abstraction from all of them . . . A substantive theory . . . is . . . about something in the real world (Diesing, 1972; p 31).

Consequently, substantive theory needs to be verified and if changes to the theory are to be made there must be references to empiricism. The formal theory ". . . can be understood and studied in abstraction . . . one can . . . make deductions, search for inconsistencies, study the effects of changes in those postulated, and add new terms without referring to anything empirical" (ibid).

In the context of this thesis, the formal theory is broadly integration theory and, specifically, neo-functionalism and intergovernmentalism. The substantive theory is being generated through an analysis of the EU life insurance industry and decision-making processes and the quantitative and qualitative data and wishes to understand or dispute the formal theories (specifically neo-functionalism and intergovernmentalism) and eventually add to, or at least, question the European integration process. Theory is open ended because as new categories or properties are generated, there is a place for them in the scheme. However, this does not incorporate total re-design. This research wished to investigate, verify, question and ideally, further understand European integration through an analysis of European decision-making processes in relation to neo-functional and intergovernmental theory.

Theory Building

"The purpose of grounded theory . . . is to build theory that is faithful to and illuminates the area under study" (Corbin and Strauss, 1990; p 24). As noted above, Glaser and Strauss (1967) considered that grounded theory was concerned with two types of theory: substantive and formal (conceptual); theory allows hypotheses and substantive concepts to emerge from the data, so analysis may identify concepts relevant to understanding the data.

> In discovering theory, one generates conceptual categories or their properties from evidence; then the evidence from which the categories emerged is used to illustrate the concept. The evidence may not . . . be accurate beyond doubt . . . but the concept is undoubtedly a relevant theoretical abstraction about what is going on in the area studied (Glaser and Strauss, 1967; p 23).

The object of research, according, to Strauss and Corbin, ". . . in a grounded theory study is a statement that identifies the phenomenon to be studied" (1990, p 38). However, this does not mean that qualitative and quantitative data are incompatible. "In many instances both forms of data are necessary - not quantitative to test qualitative but both used as supplements, as mutual verification and most important for us, as different forms of data on the same subject, which when compared with each other generate theory" (Glaser and Strauss, 1967; p 38).

Glaser and Strauss (1967) emphasised that generating theory was accomplished through the collection, coding and analysis of the data and that

these three operations were done together as far as was possible. These areas should interact continually, from the beginning of the investigation to its end. The separation of these areas hinders theory generation whereas set ideas stifle it. In this study the aim is to generate a substantive theory in relation to intergovernmentalism and specifically neo-functionalism, (formal theories) and investigate them with regard to their applicability as general theories of integration and their relevance to the EU.

Conclusion

This thesis illustrates grounded theory processes in the following ways. Firstly, a comparative analysis through the open coding of individual Member States' life insurance legislation and regulatory regimes; with the subsequent creation of a legislation/regulation table and a regulation matrix; further coding through a survey of Member State insurance industries verified and refined the matrix. This investigation raised questions with regard to how legislative differences between Member States may be resolved. Secondly, through an interview programme, process is identified and illustrated through the European Decision-Making Model. The model and the matrix provide the building blocks of the substantive theory.

Thirdly, the axial coding and selective coding processes are illustrated by the matrix and the model fitting together around the core category of European integration through the creation of the SEM. Axial coding draws all parts of the analysis together: it is the pivot or the axis of theory building. Fourthly, substantive theory is formulated through the grounded theory processes in relation to the formal theories of intergovernmentalism and neo-functionalism and these are illustrated as substantive theories in relation to realism, functionalism and integration theory which in themselves could be

understood as substantive theories of Kant's 'Civic Constitution' in *Idea for a Universal History with a Cosmopolitan Purpose* and *Perpetual Peace: A Philosophical Sketch* (Kant, 1995).

In empirical terms this thesis investigates the process of European integration through supranationality, spillover and interest groups by analysing the shifts in decision-making in terms of the European life insurance sector and the creation of the Third Life Assurance Directive. Furthermore, for this analysis: (a) Neo-functionalism and Intergovernmentalism = formal integration theories; (b) The author's theory building through the thesis = substantive theory. Finally the thesis generalises the situation regarding the life insurance industry (the substantive theory) and posits elements of both intergovernmental and neo-functional spillover in the process of European integration.

With regard to the UK insurance industry and substantive theory, certain legislation has to be effected to ensure its ability to compete in the SEM. Consequently, the need for advantageous legislation is fundamental. In this context the survey attempted to identify the industry's subjective interests on a European level and investigate how they were agreed upon. One would consider that subjective interests would be voiced by organisations that speak for their membership i.e. interest groups or large companies.

Through grounded theory techniques a substantive theory is built to enable, an understanding of integration theory and allow a greater comprehension of the SEM, European Union and European integration. Open coding and comparative analysis which initiates a survey and provides a deduction (to create an SEM Member States need to compromise their normative regulatory environments). Axial and selective coding of the phenomenon

and processes suggest further induction through interviews and participatory observation. Finally, the induction procedures illustrate the need for a further survey which allows for data saturation and an in depth understanding of the phenomenon. Throughout the analysis induction and deduction go hand-in-hand. One is continually analysing the data in the process of building theory. One is continually challenging theory through collecting and analysing data. Ultimately, ". . . methodology is the theory of methods" and the ". . . grounded theory methodology is in itself a theory which is generated alongside the substantive theory it is generating" (Glaser, 1992; p 7).

This thesis recognises the difficulty in giving precise definitions of induction and deduction and the point where the former begins and the latter ends (and *vice-versa*) and acknowledges the grey area between the two. Such is considered by Alfred Marshall when he spoke of the methods.

> You make all your contrasts rather too sharply for me. You talk of the inductive & deductive methods: whereas I contend that each involves the other & that historians are always deducing, & that even the most deductive writers are always implicitly at least basing themselves on observed facts (Marshall, cited in Coase, 1995; p 169).

Ultimately, Marshall wishes to emphasise the mutual dependency of induction and deduction as do Strauss and Glaser but each with different weighting. This thesis accepts the interdependency of induction and deduction. Effectively, such a process is at work in this research. However, there is an inclination toward emergence but an acceptance that forcing may take place unwittingly. As with the problems of delineation between induction and deduction the same may be said in respect of emergence and

forcing. The same may be said in terms of the difference between objectivity and subjectivity with emergence concentrating on the pursuit of objectivity in distance from the area under research; and forcing recognising the impossibility of pure objectivity because subjectivity is always involved in the interpretations of those undertaking the research and those being researched[2].

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[2] There is a dispute between Glaser and Strauss that revolves around the issue of the emergence and forcing of data. Glaser considers that Strauss' and Corbin's "pet theoretical code violates relevance and forces data" (Glaser, 1992; p 28). He contends that such a structured outlook undermines the emergent, empirical and endless ways of relating substantive codes. "The researcher must be aware of the vast array of theoretical codes to increase his sensitivity to their emergence in the data" (ibid). However, in their work Strauss and Corbin address their book to those ". . . who are about to embark on their first qualitative analysis research project and who want to build theory at the substantive level" (Strauss and Corbin, 1990; p 8). In other words, it is a simplification which may lead the researcher into the more difficult nuances of grounded theory.

Verification also seems to be a sticking point between the scholars. However, on closer examination neither is pursuing pure verification; each wishes for it to add to theory generation not to negate or disprove ". . . but add variation and depth of understanding" (ibid p 109). Glaser considered that the ". . .two types of methodologies should be seen in sequential relation. First we discover the relevancies and write hypotheses about them, then the most relevant may be tested for whatever use may require it" (Glaser, 1992; p 30). Whereas, Corbin and Strauss saw it as an aspect of the grounded theory method; they considered that statements should be verified against data, not to ". . . necessarily negate our questions or statements, or disprove them, rather . . . add variation and depth of understanding" (Corbin and Strauss pp 108-109). It is just as important to ". . . find differences and variation as it is to find evidence that supports our original questions and statements. The negative or alternative cases tell us that something about them is different so we must move in and take a closer look" (ibid p 109). However, each considers that it is possible to utilise verification as part of theory generation, the latter as part of grounded theory and the former as a methodology in its own right (see Strauss and Corbin, 1990; pp 107-109, Strauss, 1987; pp 11-15 and Glaser, 1992; pp 27-30).

Strauss (1987) makes his position clear where he contends that induction, deduction and verification are the very basis of grounded theory. "Because of our earlier writing in *Discovery* (1967) where we attacked speculative theory - quite ungrounded in bodies of data - many people mistakenly refer to grounded theory as 'inductive theory' (however), as we have indicated all three aspects of inquiry . . . are absolutely essential" (Strauss, 1987; p 12 authors brackets). "Grounded theory is of course inductive; a theory is induced or emerged after data collection starts. *Deductive work in grounded theory is used to derive from induced codes conceptual guides* as to where to go next for which comparative group or sub-group, in order to sample for more data to generate the theory" (Glaser, 1978; pp 37-38).

Glaser and Strauss' disagreements are based around their emphasis on deductive and inductive processes; Strauss considers that induction, deduction and verification are essential elements of grounded theory. Induction is primarily based on experience with the same kind of phenomena at some point in the past. It may be apparent because of personal experiences, exploratory research into phenomenon, previous research or because of theoretical sensitivity (knowledge of technical literature). "As for deduction: Success at it rests not merely on the ability to think logically but with the experience in thinking about the particular kind of data under scrutiny" (Strauss, 1987; p 12). This means drawing on experience as well as thinking about the phenomenon and may include comparative analysis to further the deductive powers (ibid). He also indicates that experience and learned skills are very important for verification. "If . . . experience and associated learned skills at verification, deduction and induction are central to successful enquiry, do not talent-gifts-genius contribute to that success?" (ibid, p 13).

The full extent of the difficulties emerge in the two latest works. Strauss and Corbin propose that in grounded theory there is a continual movement between inductive and deductive thinking and that their statements are deductively proposed and verified (Strauss and Corbin, 1990; p 111). There is a continual comparison of incidents ". . .there is a constant interplay between proposing and checking. This back and forth movement is what makes our theory grounded" (ibid). Glaser posits that it is at this point that Strauss and Corbin indulge in ". . .full conceptual description by forcing the data and leaving the emergence of grounded theory out completely" (Glaser, 1992; p 71). The sticking point is the confusion between induction and deduction. Glaser charges that he (Strauss) ". . . confuses induction with testing deductive hypotheses which are forced on the data (and) that it is not inductive to say the data disproves an hypothesis, it is simply a verification (ibid). However, Strauss and Corbin contend that it is necessary to continually verify ". . . concepts and relationships arrived at through deductive thinking must be verified over and over again against actual data. . . we are building grounded theory and it is the grounding or verification process that makes this mode of theory building different" (Strauss and Corbin, 1990; pp 111-112). In response to this Glaser charges that Strauss and Corbin are developing a verificational method. "It simply tests forced conceptual hypotheses"

Finally, one may consider, that grounded theory should be interpreted as it was by Glaser: "By its very nature grounded theory produces ever opening and evolving theory on a subject as more data and new ideas discovered. This nature also applies to the method itself and its methodology" (Glaser, 1978; p ix).

Glaser wrote that the ". . . analyst must remember it is the idea he is using not the person it was borrowed from . . . it is only a slight easy step for the analyst to get lost in referring to the man and his work and to forget the theory being generated and the work it took to establish an emergent fit (Glaser, 1978; p 8). Strauss considers he took the idea further Glaser disagreed. Interpretation is everything? "Interpretation is grounded in something we have in advance . . . understanding operates in . . . an involvement whole that is already understood". Effectively the environment or background determines possible ways of questioning. However, interpretation is also ". . . grounded in something we see in advance - in fore-sight" (Heidegger, 1962; p 191). Additionally, interpretation is made on the basis of those around you through symbolic interaction. Indeed, one is both subjective and objective in this context. Interpreted by self in relation to society and interpreted by society in relation to self, that is through self-indication[3]. "Self-indication is a moving communicative process in which the individual notes things, assesses them, gives them a meaning, and decides to act on the basis of meaning" (Blumer, 1962; p 183). However, to accomplish this some fore-sight is necessary, even if it is only a comprehension of language or culture.

(Glaser, 1992; p 92). It is not a method that generates theory but one that verifies; it is a theory that forces the data rather than allowing it to emerge. For Glaser it was crystal clear that Strauss and Corbin had created a verification method.

[3] There is a great deal of scope for research to identify the links between phenomenology and the pragmatic approach of symbolic interaction in relation to different methodologies. However I am afraid it is beyond the scope of this thesis

This is how the author has approached the data, with the acknowledgement of social interaction and foresight. Foresight takes into consideration the theories that already exist regarding integration and specifically European integration. These are perceived as formal theories. Additionally, the researcher brings to the analysis expertise, knowledge and theoretical sensitivity. However, also bringing minimal preconceptions especially in the form of deduced *a priori* hypotheses. Effectively, objectivity is continually pursued through the recognition of subjective influences throughout the research process.

The main aim of the thesis is to develop a substantive theory and use it to further our understanding of the European integration process. Indeed, the ". . . research findings constitute a theoretical formulation of the reality under investigation rather than consisting of a set of numbers or a group of loosely related themes. (Corbin and Strauss, 1990; p 24). To do this the thesis analyses the harmonisation and integration processes in a specific service sector and relates the findings to a number of formal theories; and specifically the formal theories of intergovernmentalism and neo-functionalism. This thesis's concept of theory is taken further in the following chapter.

Chapter Three

Formal-Substantive Theory?

Elements of Integration Theory

> *Theory is always for some one and for some purpose. All theories have perspective Perspectives derive from a position in time and space . . . Of course, sophisticated theory is never just the expression of perspective. The more sophisticated a theory is , the more it reflects upon and transcends its own perspective; but the initial perspective is always contained within a theory and is relevant to its explication (Cox, 1981; p 128).*

Introduction

This chapter provides an analysis of theory and illustrates the differences between formal and substantive theories through an overview of integration theory. It indicates how the grounded theory understanding of theory building will be used in this thesis. And through this approach it illustrates how a number of difficulties with integration theory and especially neo-functionalism may be overcome.

"Virtually every major international relations theory has been criticised because it does not successfully predict outcomes" (Luchner, 1992; p 34). Effectively, the subject area is saturated with ideological stances which continually slant the debate. "Depending on who is arguing, it is either power theory, integration theory or interdependence theory that is not precise enough" (ibid, p 43). Haas criticises power theory and questions its use as

either a guide for the states person or as an analytical theory. Keohane and Nye, whose theory of interdependence owes much to integration theory, argue there is no such thing as integration theory but only integration studies. (cited in Luchner, 1992). However, is this not the difficulty of all analysis within the social sciences? Luchner asks ". . . are international relations scholars . . . continually reinventing the wheel, and if so why do we keep repeating ourselves" (ibid p 36). Why indeed? Is it not to develop better theory? If we are to build theory, do we not have to build on what is already there? Without past theory and the continual reassessment and re-analysis of it we have nothing. Of course, this raises questions of how theory as a concept may be defined. In the strictest sense, theory should have shared assumptions and predict outcomes. However, the extent of prediction and the methods that should be applied are serious bones of contention not only in integration theory but in most social sciences. All that can be said of most prediction in the social sciences is that they are generalisations or trends: to expect more would be to crave omnipotence. This illustrates a shift from the naive realism of *positivism* to the critical realism of *postpositivism*[1].

The more information one has regarding the likelihood of an event, the greater the generalisation may be. At present, EMU is far more likely to take place in the EU than political union. However, with the actuality of EMU, political union becomes more likely and generalisation in this direction more feasible i.e. the chance that it may be realised in one form or another becomes more realistic. Additionally, to contend that political union will definitely occur 12 months following EMU is unacceptable, but to consider political

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[1] Positivism and postpositivism are paradigms of inquiry. Positivism considers that an apprehendable reality exists through which immutable and natural laws may be derived. Postpositivism also considers that reality exists but it considers that because of the human condition (the flawed human intellect) it cannot be apprehended perfectly. Consequently, reality must be subjected to wide critical examination so it can be understood as near as possible (but never perfectly). Of course, definitons of theory are different when understood from a critical theory or constructivist perspective. This analysis remains in the postpositivist paradigm in its use of grounded theory.(see Guba and Lincoln, 1994).

union as a probability is far more realistic (which in itself is a generalisation). Consequently, the methodology used in this thesis posits that theory is not simply about predicting: it also deals with understanding and generalisation. Theory is never completed but continually added to. Ultimately, this thesis builds a substantive theory in relation to formal theories through grounded theory techniques.

To fully comprehend different ideas of neo-functionalism, it is worth noting the theories that generated it and are juxtaposed to it: these are federalism, and functionalism. Additionally, there is a school of thought that considers that any integration must be brought about by the nation-state. This is normally known as a realist understanding of international relations and is one that underpins intergovernmentalism.

Firstly, this chapter discusses Kantian political thought to identify the underpinnings of federalism and functionalism. Secondly, it indicates how intergovernmentalism draws on realism. And finally, the chapter illustrates how neo-functionalism is akin to aspects of federalism and functionalism. Overall, this chapter will give an overview of the particular theories in relation to Kantian political thought and integration theories (functionalism, federalism, realism, intergovernmentalism and neo-functionalism) and provide some general principles.

Kantian Political Thought; Universal History and Perpetual Peace

In his work *Perpetual Peace a Philosophical Sketch,* Kant considered that no ". . . conclusion of peace shall be considered valid as such if it was made with a secret reservation of the material for a future war" (Kant, 1995; p 93). Indeed, a suspension of hostilities does not guarantee a lasting peace. Kant considered

that to achieve perpetual peace, it is necessary for it to be formally instituted and this needed to be concretised in a legal civil state. Such a legal state should be based on a constitution which is founded on three principles ". . . firstly, the principle of *freedom* for all members of society (as men); secondly, the principle of the *dependence* of everyone upon a single common legislation (as subjects); and thirdly, the principle of legal quality for everyone (as citizens) . . . a constitution based on cosmopolitan right, in so far as individuals and states, co-existing in an external relationship of mutual influences, may be regarded as citizens of a universal state of mankind (*ius cosmopoliticum*)" (ibid, pp 98-99). This idea was first illustrated eleven years earlier in *Idea for a Universal History with a Cosmopolitan Purpose.* In this, Kant purports nine propositions that indicate a guiding purpose for history.

In *Universal History,* Kant considered that ". . . all natural capacities of a creature are destined to evolve completely to their natural end . . . (and) . . . the unsociable sociability of man" moving toward the ". . . achievement of universal civic society which administers laws among men" is the highest problem nature assigns to humanity (ibid, p 16 author's brackets). Only once a civic society has been attained can nature's other problems be solved. Humans need to exist within society because this creates a feeling of being more than human (as more than the developed form of their natural capacities). At the same time humans are unsociable because they feel hostility to those around them and expect hostility in return. It is this process that forces humans to protect themselves by aspiring to hold rank among their peers. Need forces humanity into curbing its natural aspirations to ensure a peaceful existence, unsociability initiates the "just civic constitution" and this incorporates laws to which all are answerable and no one is above. However, Kant recognised that one nation may attain a "just civic constitution" but unfortunately antagonisms would still exist between states

(ibid). "The problem of establishing a perfect civic constitution is dependent on the problem of a lawful external relation among states and cannot be solved without a solution to the latter problem" (ibid, p 18). Each state will expect the same antagonisms which forced it into seeking its own civic constitution. Through war and the threat of war, the full potential of humanity cannot be realised: consequently humanity is forced to seek the means of ensuring an equilibrium. Through self-interest humanity is forced to accept mutual existence. This thesis considers that this is the basis of European Union: mutuality and peace created through self-interest.

The theories in this thesis investigate past attempts at equilibrium, and those being pursued in the present, with an emphasis on peaceful co-existence in the future. The concept of the league of nations and a united Europe was initiated through such an attitude i.e. the pursuit of a civic constitution to ensure peace between nation-states. The premise of the European Coal and Steel Community (ECSC) was peace: its objective was to alleviate the prospect of war in Europe by controlling the products necessary to conduct a war. Through the pursuit of peace, Kant perceives a world civic constitution and as indicated above, this thesis contends that Europe fits into such an understanding in that it is an evolutionary or dialectical movement away from the nation-state toward such an entity.

Integration Theory

Political integration may be perceived as a situation in which two or more entities form a new structure (Galtung 1968). In international terms, we are speaking of nation-states undergoing a form of metamorphosis: in other words, they do not have to change into the same thing (another larger nation-

state). As indicated by Kant, integration may create world government or some type of regional federation like the EU.

On such a process, most integrationist theorists would agree. However, a problem arises when we examine the kind of political community to be aimed for and the strategies and conditions that allow integration to proceed. In the first case, there are those who consider that integration encapsulates the formation of a supranational entity and those who press for the interaction of peoples across geographical boundaries. The former may be seen as the federalist or the state model while the latter represents the functionalist or community model. In the second case, the problem is apparent for academia and the policy-makers alike: academics tend to concern themselves with the identification of independent variables that account for the process of integration, whereas politicians concern themselves with the tactics and strategies of political change: i.e. how does one engender and achieve a process of integration?

Some consider that successful integration depends on the bargaining power of political elites and their abilities to reach compromises acceptable to the public. Others consider that technology, the economy and social entities drive the integration process. The political outcome is not determined by these elements but makes demands on existing structures and allows opportunity for political bargaining out of which an integrated community may gradually emerge (Pentland, 1975).

Realism and Intergovernmentalism

The debate at the international level revolves around the realist argument and the functionalist argument. Realism is based on the Hegelian

interpretation of the state and international relations. "International law springs from the relations between autonomous states . . . The nation-state is mind in its substantive rationality and immediate actuality and is therefore the absolute power on earth" (Hegel, 1967; p 212). The intergovernmental critique emphasises the importance of the nation-state in the process of European integration and is based on a realist model and Hegelian understanding of international politics.

For realism, theory consists in ascertaining facts and giving them meaning through reason. It assumes that the character of a foreign policy can be ascertained only through the examination of political acts performed and of the foreseeable consequences of these acts. Thus we can find out what statesmen have actually done, and from the foreseeable consequences of their acts we can surmise what their objectives might have been (Morganthau, 1973; p 4).

Based on the concept of power, realism is encapsulated by the motives of nation-states. Effectively, international relations in the form of foreign policy are pursued by nation-states alone. Consequently, these are the motors of change. However,

> . . . political realism does not assume that the contemporary conditions under which foreign policy operates, with their extreme instability and the ever present threat of large scale violence cannot be changed . . . Nothing in the realist position militates against the assumption that the present division of the political world into nation-states will be replaced by larger units of a quite different character, more in keeping with the technical

> potentialities and the moral requirements of the contemporary world (ibid, p 9-10).

But this may only be achieved through the forces at a territory's disposal and these forces are encapsulated by the nation-state. "The realist cannot be persuaded that we can bring about . . . transformation by confronting a political reality that has its own laws with an abstract ideal that refuses to take those laws into account" (ibid, p 10). The questions are: will the nation-state make itself obsolete? And do such laws or such a reality actually exist? Indeed, Keohane and Nye (1977) argued that ". . . integration among states is slight and lasts only as long as it serves the national interests of the most powerful states. Transnational actors either do not exist or are unimportant" (p 24).

The realist model identifies international politics as continually in a state of conflict, as dominated by struggle. Four assumptions underlie a realist understanding of international relations:

> (a) States are the dominant protagonists in international politics.
>
> (b) States act as coherent units.
>
> (c) Force is an effective instrument of international policy.
>
> (d) High politics such as foreign policy and military security will always out weigh low politics e.g. economic policy.
>
> (Morganthau, 1973; p 10)

Based on the realist critique, intergovernmentalism considers a number of points. Firstly, it considers that regional integration should take global criteria into account. Secondly, it contends that the real power-houses in the process of European integration are the nation-states and that these would remain committed to national interest. Finally, intergovernmentalists think that the

transference between low and high politics will never take place; integration would be condoned in technical fields to ensure mutual benefit but would never move into areas like defence, monetary policy and national security (George, 1994).

There is no need to dispute the first of these points as everything is affected by international variations and historical change. The second of these assumptions denies the neo-functional idea: that through sector bargaining the political process would shift from the national to the supranational and overcome the dichotomy that the realists create for themselves. Indeed, the realists consider that things will change, but only through the perpetuation of what already exists (the nation-state). However, if the EU encompassed a larger nation-state, then in this context it would fit into the intergovernmental perspective. The third assumption may be disputed with the potential advent of monetary union and the extensions of decision-making powers that the European institutions have incrementally accrued. Richardson (1996) argued that it was necessary to take low politics as seriously as high politics. Indeed ninety per cent of European integration is about low politics and to fully comprehend this process it is necessary to understand how a range of non-governmental actors interact and how low decisions and policies evolve into legislation. European integration is ". . . not simply the outcome of inter-state bargaining . . ." (p 5) but a complex process involving numerous actors. However, modern government is not ad-hoc but a procedural means of dealing with different preferences. Thus, such procedures may involve neo-functional as well as intergovernmental processes.

Federalism

Federalism has developed through Kantian ideas, the Enlightenment, the federalist Papers of the Philadelphia convention and British nineteenth century thinkers (see Friedrich, 1967; Hodges, 1972; Levi, 1991; Katz, 1991; Pinder, 1991; Bosco, 1991). With regard to its European perspective it was ". . . designed to explain why the European polity *ought* to have a federal system, particularly in the aftermath of WW II" (Luchner, 1992; p 50). However, the proponents of a federal Europe did not give enough thought to how a federation may be attained. Unlike functionalism which followed incremental steps toward integration, ". . . most federalists initially implied that the best path towards integration would be a meeting akin to the Philadelphia convention where a written constitution for the European Federation could be drawn up" (ibid, pp 51-52). Initially, federalism was perceived as a theory of war and peace. Continued harmony between independent unconnected sovereign states in close proximity to each other is not borne out by historical experience. Fundamentally, ". . . historical experience teaches that peace cannot be maintained among sovereign states. Peace requires federation" (Levi, 1991; p 32). Re-iterating Kant's ideas in *Perpetual Peace,* Levi contends that,

> . . . peace is not merely a negative state of affairs, i.e. the suspension of hostilities in the interval between two wars. It is a positive situation which rests on a specific political organisation, i.e. federation. It does not depend on goodwill. It can only be achieved by a legal order and by a democratic government with independent legislative, executive and judiciary bodies (ibid).

However, whether European Union ". . . will assume the character of a federation, whether it will be a historically unprecedented political community, or a slowly developing 'untidy' federation, is not yet known" (Luchner, 1992; p 51).

Change in federalism occurs when the historical circumstances are right and transferral is brought about by political elites alone. Compromises are reached and new institutions formed: all this occurs with an element of public support. Federalists consider integration to be the formation of a supranational state, which is given form through constitutional authority being realised in the new state. This is usually illustrated through a comparison with the United States as an ideal type and the contention that ". . . the emulation of a process that supposedly aided the United States to become the dominant power in the wake of World War II" (ibid, p 52) would enable a United States of Europe which could counter the American challenge. In this context, there are links with intergovernmentalism in that federalism pursues the creation of a larger new state. Indeed, such considerations counter the premise of European Union (peaceful co-existence) and such an understanding would consider that the EU would perpetuate conflict. Additionally, the adherence to ideals can lead to impromptu conclusions about the success or failure of the integration process, because ". . . ideal types are not true dependent variables since they cannot yet be observed or measured in nature" (Haas, 1971; p 27).

Federalism looks to both unity and diversity and draws on the need to pacify nation-states through the practice of federal government. Its supporters claim it to be a superior form of government in that there is the possibility of reaching world government with the minimal dilution of national identities; once again adhering to certain intergovernmental principles.

Finally, moderate federalism or neo-federalism, as it has been labelled, also aims at constitutions. However, neo-federalists illustrate greater interest in the integration process than their counterparts. Effectively, they think beyond the construction of a United States of Europe and adhere to the concept of regionalism. Fundamentally, they consider that ". . . the European nation state as the strongest European political unit, has to fear a loss of power not only because of centralisation of power in EC institutions but also because of a possible devolution of power to regional polities" (Luchner, 1992; pp 54-55)

Overall, federalism is perceived as a model to be aimed for, either in the more general understanding of a United States of Europe, or as a more devolved unit as illustrated through subsidiarity, the conception of which is included in the Maastricht Treaty (Article 3b). Federalism is most usually associated with the theory of federal government. However, there are those who consider that federalism is more a way of thinking and acting and consider that federalism is an ideology. It is seen as an ideology with a view of a political pursuit that would ensure a precise social existence. Such was indicated by Albertini (1979) who considered that federalism can only become apparent in ". . . multi-state areas which have reached the material and ideal conditions for political freedom . . . (only when the area is) . . . at a stage of development of material production, and of the consequent human interdependence, in which the division of society into classes has already been overcome, and in which it is possible to overcome the division of humanity into nation-states" (Cited in Bosco, 1991; p 15).

Albertini provides a general federalist theory and indicates three elements of federalism:

(a) A particular historical time, a period where class antagonisms had been overcome and national antagonisms were about to be overcome;

(b) A general moral stance, the concept of peace;

(c) A structural denotation, a federal government.
(ibid).

This is taken further by Levi who contends that the underlying principle of federalism is democracy and that further federalism requires a new stage in democratic government.

> Federal institutions open new possibilities in the struggle for peace. The achievement of international peace requires a new stage in the enlargement of democratic government . . . The first stage was ancient democracy . . . The second stage is representative democracy . . . The third stage is federal democracy. Federal democracy is designed to establish peace among nations and continents. Federal institutions give mankind a new power, the power to build a democratic state as big as the world This was the discovery of the United States constitution. That constitution concerns only part of the world, but now it must be applied to the other continents which have not yet achieved political unity (European Community first of all) and to the whole world (strengthening and reforming the United Nations) (Levi, 1991; p 33).

With regard to European integration, federalism enables the formation of a common goal and offers an understanding of institutional integration that

may be compared with historical processes. Additionally, neo-federalism recognises the importance of the regions and incorporates this in its approach to integration. Finally, on some issues there is a close relationship between federalism and neo-functionalism and these will be highlighted in the conclusion of this chapter.

Functionalism

Mitrany (1943, 1944, 1965, 1970, 1975a, 1975b, 1975c) concentrated on international institutions and perceived their existence as a means of international divisions being overlaid by inter-state agencies through which the interests of countries would gradually be integrated. The premise of the process was benefit: international welfare would overcome emotional attachment to the state and provide international institutions which would engender both prosperity and peace. Mitrany gives the example of the international organisation of communications as a functional heading e.g. railway communications would be administered at the "logical limit of co-ordination" obviously at the level of the continent. "Shipping, on the other hand, would be administered on inter-continental terms but not universally. Land bound states would have little to offer the function of the organisation. Telecommunications, broadcasting and air travel would be organised on an international scale" (Mitrany, 1975a; p 116). Effectively, administration should be undertaken at the most logical level to enable efficient functional decisions.

Mitrany considered that the two main objectives of government were stability and the management of change. "As regards the first it would not be difficult constitutionally if the political will were there, to translate the instruments and experience of national life into the needs of the international order; but

with regard to peaceful change the problem in the two spheres is utterly different" (ibid, pp 131-132). The task was perceived as the building up of a common interest in peace. However, universal organisations in the context of the League of Nations and the United Nations were not yet achievable, and this was born out by their failure. Mitrany acknowledges the federal system on the one hand but sees it of limited scope, and in logical terms ". . .at the expense of general unity" (Mitrany, 1975b; pp 121-122). For Mitrany, functional organisation would create integration and peace.

As it became more apparent that the nation-state was able to assume, quite adequately, a wide range of welfare functions to ensure the well-being of its people. This led to a rethink of the state's position in the functionalist process. Indeed, it was concluded that rather than by-pass the state, it would need to be an element in the integration process. The welfare aspects of the state could be integrated on, if not world, then a regional basis; this was a shift from functionalism to functional integration (Mitrany 1944).

It may be argued that functionalism allows for the changes and adaptations that social evolution creates: that it is pointless to work towards some specific end as is attempted in a federalist model because humanity is incapable of delineating the end point. All one may achieve is a concept of community that indicates organisational networks each designed to meet a specific social, economic or technical need. Functionalism looks to change through ". . . linking authority to a specific activity and seeks to break away from the traditional link between an authority and a definite territory" (Mitrany, 1975a, p 125).

In 1943, Mitrany considered that the ". . . new approach toward the goal of international collaboration is free from dogma . . . and offers a line of action

that might overcome the deep-seated division between the needs of material unity and stubborn national loyalties" (ibid, p 126). Mitrany provides a broad test for moves toward an international order, the means by which change is brought about and aptness of the change to the given time. This is also illustrated in the organisations necessary, each of which would be designated a specific task that would not remain static but evolve as the functional need changed. A political dimension would exist to direct the network e.g. in terms of planning and interaction. Through this process it was hoped that a system of peaceful co-existence would emerge. Through interdependence and the multi-involvement in solving socio-economic problems, the psychological and material bases of war may be alleviated.

At the very least, the structure could be a pluralist international community where national control is marginalised through functional linkages; or one of greater extremity where the nation-state disappeared and was replaced by an international administrative body where organisational patterns were determined by functional rationality.

As far as functionalism is concerned, the process of integration may be initiated at the intergovernmental level or at the transnational. Governments that cannot deal with international problems single-handedly or groups that have similar interests may create functional organisations. In either scenario, the main impetus of organisational growth is 'technical self-determination'. This incorporates the increasing autonomy of technical organisations in that ". . . administrative convenience and efficiency demand that an expert body be not unduly hampered in its investigations by the necessity of constantly new instructions and authorisations" or as Mitrany put it ". . . certain agencies are born with or achieve 'functional autonomy' by

virtue of the desirability of such an autonomous status" (cited in Sewell, 1966; pp 250-51).

Functional 'needs' in the expression of 'demands' by social groups indicate social and structural goals that incorporate a means by which these structures may be met. These directions are adhered to by governments and experts which illustrate common needs rather than individual power. Functionalism is about building communities through collective education and technocratic management: it is based on the understanding that nation-states exemplify political tension and pressure and if they are not to lead to a catastrophe international political integration must take place. The beneficiaries of this process would exemplify greater support for the integration process and further co-operate as the process intensified.

Functional theory constitutes:

> ". . . a body of propositions (still interconnected) which serve to map out the problem area and thus prepare the ground for its empirical investigation by appropriate methods. More precisely, the propositions serve to classify phenomena, to analyse them into relevant units, or indicate their interconnections and to define rules of procedure and schemes of interpretation. Theory here equals conceptual scheme or logical framework" (Haas, 1964; p 7).

In this context, functionalism is a scheme of procedure, a scheme of interpretation and a theory: a conceptual scheme or a logical framework.

Haas (1964) contended that disharmony prevails where authority is exercised by politicians rather than interest groups: that things can only improve when the government of humans is replaced by the administration of things. He points out that there is little hope of achieving a general state of welfare when human loyalties are bound to the nation-state. Once freed from a position of national insecurities, humanity would be able to strive toward the good of all. Functionalism is interested in bringing states together to engender peaceful co-existence, to actively encourage a state of peace. Efforts are initially directed toward economic and social reform in a bid to remove the causes of conflict. Welfare, rather than power, incorporates the functionalist ideal and technocrats concentrating on specific areas rather than polity would take centre stage. Technical interests would eventually become fused and this would engender change.

Functionalism accepts that the concept of the nation-state will be difficult to overcome especially in respect of a move towards some form of world community. Most concede that the concept of a world community will be unrealistic until the idea of a world citizen is apparent. Likewise, with the EU: until the idea of the EU citizen becomes a reality true union will be difficult to achieve. On the one hand, Europe may be interpreted as an evolutionary link in the functional process, whereas, on the other, it could be perceived as dysfunctional in that it creates no more than another super-state which would add to rather than detract from the world's problems. However, functionalism and neo-functionalism are similar in that they stress:

(a) Economic welfare.

(b) Technical co-operation.

(c) Utilitarian factors of integration.

(d) Prerequisite of a pluralistic social setting.

(e) The role of technocrats.

The two theories differ over the dynamics of integration rather than the result; functionalism adheres to a community model, whereas neo-functionalism primarily subscribes to a supranationalism.

Neo-functionalism

Neo-functionalism considers the integration process to be one where political actors are persuaded to allocate their loyalties and political activities towards another setting. Political actors are persuaded to do this through pressures from organised groups that express demands for further integration. The neo-functionalist model does not need overall consent: it is driven by self-seeking interest groups who are restrained only by the acceptance of the rules of the game, rules they themselves have a hand in creating. It has been posited that integration results through the process of institutionalised patterns of interest group politics undertaken in existing organisations. (Haas, 1964). The self seekers in this thesis are the individual Member State life insurance industries and companies.

Haas (1958) presented the European dimension as one where

> . . . political integration is the process whereby political actors in several distinct national settings are persuaded to shift their loyalties, expectations and political activities toward a new centre, whose institutions possess or demand jurisdiction over the pre-existing national states. The end result of a process of political integration is a new political community, superimposed over the pre-existing ones (p 16).

This stance accepted the concept of supranationalism and condoned the pursuit of a united Europe through functionalist means. However, not all neo-functionalists agree with the federal model as this seems to deny other outcomes; following the stagnation in European integration over the 1960s theorists have described integration in different terms. Haas described integration as leading to a common decision-making process among a group of states (Haas, 1971).

The functional model lies at the heart of the neo-functional view of the integration process. Through observing the European Coal and Steel Community (ECSC) and the European Economic Community (EEC) it was agreed that the process of integration could not simply be explained in terms of technical self-determination and the learning of co-operation. Out of the acceptance of such came the set of ideas that underpin neo-functionalism.

Haas (1958) provides an outline of neo-functionalism. Political parties and interest groups accept that action should be taken at the supranational level. Interest groups and political parties organise and function beyond the nation-state and define their interests in the new environment. Interest groups and political parties through their interaction sow the seeds of ideological agreement which overtake those based at the national level. There is an adherence to the rule of law by the parties involved which include governments and interest groups, and when decisions are opposed dissatisfactions are channelled through legal avenues rather than issuing threats or ignoring the situation (Haas, 1958).

There needs to be a reassessment of European integration's lost theory (neo-functionalism) if it is to be fully understood. Recently, some neo-functional

thinking has found ". . . its way back into our theorising after almost twenty years of neglect (which) indicates that judgements on integration theory were at times a bit too general" (George, 1994; pp 40-41 author's brackets). Additionally, Keohane and Hoffman (1991) have argued that many of Haas's ideas in respect of neo-functional processes have been open to distortions in the contemporary literature (George 1994). Hence there is a need to revisit neo-functionalism and assess it in relation to other integration theories. Consequently, the next chapter will analyse neo-functionalism in some detail before the thesis moves onto the empirical work.

Conclusion

This chapter has outlined five theoretical schools, each of which encapsulates different values and goals. This investigation incorporates different elements of each theory, but relies heavily on an analysis of neo-functional and intergovernmental processes of change. It is apparent that functionalism, federalism and neo-functionalism have their roots in Kantian political theory. Where, realism and intergovernmentalism are more closely bound to Hegel. However, each attempts to understand international relations and proposes a means of generating a democratic international society.

Federalism is apparent in the result that some proponents of European Union identify, i.e. a federal state (it is recognised that federalism accepts a world order, but this does not need to follow a defined European state). Functionalism is the general trend of areas of common interest creating reliance on each other in the international sphere. Neo-functionalism provides for the general functionalist theory to be used on a regional basis (in this case the EU). In so doing, it allows a supranational entity and spillover and emphasises interest group interference in the decision-making process.

This does not mean that the international perspective has to be discarded: the supranational body could be perceived as a means of transition from the national toward a larger entity. Indeed, this could be the dependent variable that intergovernmentalism might pursue. A larger nation-state, it is only the process that would be disputed.

As an integration theory, neo-functionalism utilises aspects of pluralism, federalism, legalism and functionalism and allows an analysis of a specific creation, the EU. Neo-functionalism allows an adaptation of functionalism in that it provides a means by which the construction of propositions about regional integration may be understood. It allows for a dialectical shift away from the nation-state toward a supranational unit, the dimensions of which are to date unknown.

Federalism	European Union as state/then shift to world order through constitutions.
Functionalism	Coincidence of common goals through international institutions.
Neo-functionalism	Coincidence of common goals at regional level in federal/constitutional and plural terms through a functional/institutional spillover/supranational process.
Realism	Power politics initiate the motives of nation-states. Larger units may be brought about but these will only be created by and become larger nation-states.
Intergovernmentalism	The major propellant in the shift toward European Union is the nation-state. Similar to a realist perspective, but at the EU level.

In realist and intergovernmental terms, international society is depicted as divided by conflict, nationalism and high politics (defence, foreign policy, etc.). In functional and neo-functional terms, successful integration processes are described in terms of education, or the perceived advantages of a shift away from national governments that are learnt through experience. In the integration process they are tempted away from the national level through realising the advantages of co-operating at the international or, in the case of neo-functionalism, at a regional level. (Taylor, 1968).

Functionalism is peace-oriented and through an emphasis on co-operation and integration looks towards a world system. As outlined in the introduction, this author considers that the process is built on the Kantian concept of "a just civic constitution" (Kant, 1995).

Neo-functionalism is a theory of international relations and affects our understanding of the international environment. Haas considered that the

> . . . search for world order is nothing but an attempt to conquer turbulence. Theories of regional integration have a lot to teach us still about non-violent methods for collectively solving international problems, for coping. They can find a place in the intellectual armoury of studying alternative world orders. But this armoury must be stocked with new concepts as well. I shall suggest that this process has begun in the European Community at the level of policy, and that these policies and the institutions devised to implement them *illustrate the attempt to deal with turbulence rather than deal with political integration* (Haas, 1975; p 180).

Functionalism identifies aspects of human interests needs and desires. Haas (1964) identifies function as the needs and purposes which relate the organisation to its environment. Out of this arises the concept of system: ". . . do we look for the impulse generating organisational action in the organisation itself or in the environment?" (Haas, 1964; p 7).

This thesis concentrates on the operation of the changing life insurance industry. This is examined, on the one hand, as a social organisation in transition and on the other as an entity that through integration is involved in changing its own social environment. The analysis has identified a changing process through the Third Life Assurance Directive, how this was agreed upon and the compromises that each Member State industry needed to make to achieve the new environment. This, it is considered, is a process of integration. The thesis concentrates on the process of intergovernmentalism and neo-functionalism in the field of European integration and the extent to which these may be considered as means of integration. Consequently, the next chapter will explore neo-functionalism in terms of its credibility as a means of understanding European integration processes in relation to those of intergovernmentalism.

Chapter Four

Intergovernmentalism, Neo-Functionalism and European Integration

A conclusion of peace nullifies all existing reasons for future war, even if these are not yet known to the contracting parties (Kant, 1991; p 93).

Introduction

Neo-functionalism and intergovernmentalism were the two main contending European integration theories during the sixties and by the seventies it seemed evident that the latter had won the argument. However, the mid-eighties and early nineties have seen a resurgence in the integration process and this thesis contends that once again attention has been turned toward neo-functional processes. "The Single European Act led to a revival of neo-functionalist explanations . . ." with regard to European integration (George, 1994; p 1). Indeed, it was considered that the abandonment of neo-functionalism ". . . left the study of European integration in a theoretical void . . . however, neo-functional concepts are again appearing in the writings of some EC-specialists" (Tranhome-Mikkelsen, 1991; p 2). Kirchner (1992) continues the debate when he identifies two contesting understandings of European integration in neo-functionalism and intergovernmentalism. "The former sees the progression of the EC as confirmation of the cumulative logic of sector spillover and an increasing transfer of competencies from the national to the EC level. Intergovernmentalism, on the other hand, stresses that the pace and direction of EC co-operation is in accordance with national interests and is achieved through arrangements such as the Council of

Ministers and the European Council over which member states have full control" (p 35).

Intergovernmentalism, State-Centricism and European Integration

The process of European Union policy making is not purely neo-functional,

> . . . all negotiation and coalition-building takes place within the context of agreements between governments . . . successful spillover requires prior programmatic agreement among governments, expressed in an intergovernmental bargain. Such a bargain is clearly important in accounting for the Single European Act (Keohane and Hoffman, 1991; p 17).

However, this does not mean that an intergovernmental perspective provides a complete picture of European integration, but that these inter-state agreements do underpin many of the conditions necessary for European integration. There is an interaction taking place between the need for furthering the ability to trade freely throughout Europe and the political concessions to allow this. When the UK agreed to the SEA, it did so to further *self-interest* not to show ideological unity with Europe. Margaret Thatcher emphasised this when she was asked why she had agreed to the SEA: ". . . we wished to have many of the directives under majority voting because things which we wanted were being stopped by others using a single vote. For instance, we have not yet got insurance freely in Germany as we wished" (Financial Times, May 19 1989; editorial, cited in Keohane and Hoffman, 1991; p 17). However, what pressure was being put on the government by the insurance sector in particular and business in general? And does this interaction indicate a neo-functional understanding of the process? Two

elements of neo-functionalism continually recur in the process of EU reform: the pressure exerted by EU institutions and the uses of transnational business interest groups (such as European-wide interest groups). Consequently, it may be argued, that in theoretical terms we are observing an amalgamation of the two approaches.

Moravcsik (1991) denies that neo-functionalism is part of the process, ". . . by testing and rejecting a particular variant of neo-functionalism, supranational institutionalism, which rests on the argument that international institutions and transnational interest groups play a vital and increasing role as integration progresses" (ibid, p 75). He posits an "intergovernmental institutionalism" and argues that the primary source of integration is to be found with the Member States and the influence they wield in Brussels (ibid). However, even this explanation is incomplete and warrants further research. This is taken further in Moravcsik (1993) where he considered that ". . . the EC can be analysed as a successful intergovernmental regime designed to manage economic interdependence through negotiated policy co-ordination" (ibid, p 474). Indeed, he attempted to illustrate the limitations of neo-functionalism and present the theory of liberal intergovernmentalism, ". . . a liberal theory of how economic interdependence influences national interests and an intergovernmentalist theory of international negotiation" (ibid).

The intergovernmental approach adheres to the state-centric model. This considers that the ". . . overall direction of policy making is consistent with state control" (Hooghe and Marks, 1997; p 22). Furthermore, " . . . the core presumption underlying the state-centric governance model is that European integration does not challenge the autonomy of nation-states. "State-centrists contend that EU membership preserves or even strengthens state sovereignty and that European integration is driven by bargains among member-state

governments . . . In this model, supranational actors exist to aid member states to facilitate agreements by providing information that would not otherwise be available. Policy outcomes reflect the interests and relative power of member-state executives, not those of the supranational actors (ibid, p 21. For more on this see Mann, 1994; Millward, 1992; Streeck, 1996 as well as Moravscik, 1991 and 1993).

If the state-centric model is the dominant means of decision-making in the EU, three conditions would need to hold: Member State representatives in the Council of Ministers should be able to impose their understandings and preferences on other European institutions; Member States should always be sovereign in relation to other Member States; Member States should be able to control sub-national interests (Hooghe and Marks, 1997).

Garrett and Tsebelis (1996) argued that intergovernmentalism has ". . . tended to focus on the bargaining between national governments over the outcome of treaty negotiations. The epochs that treaties demarcate are considered a function of governments' preferences and their ability to further those preferences in inter-state bargaining" (p 269). Following the SEA and QMV intergovernmentalism started to look at the mechanics of EU decision-making. However, analyses concentrated on the Council of Ministers and most studies that ". . . focus exclusively on dynamics within the Council of Ministers are likely to misperceive most policy dynamics" (ibid p 293). Indeed, there are a number of problems with the intergovernmental approach: firstly, an analysis of treaty bargaining only scratches the surface of the process of European integration. Secondly, it considers that all decisions are created and made in the Council of Ministers. Both of these problems stem from intergovernmentalism's fundamental premise that " . . . all decisions are products of bargaining among nations" (ibid, p 294).

This thesis explores whether the intergovernmental approach and state-centric governance alone are sufficiently able to explain integration fully. Indeed, it turns to neo-functionalism and multi-level governance as means of allowing a greater understanding of the process.

Neo-functionalism and European Integration

Neo-functionalism is considered to be a peaceful process toward the creation of larger peaceful political communities. This is different to communication theory (Deutsch, 1954) where the process of integration may be violent but the outcome is peaceful[1]. In this context, one is separating the concept of European integration from the process of integration in general.

> The rationale for separating the general concept of integration from that of European integration has its roots in the need for a theoretical framework that is applicable to both historical cases of integration and the unique process of European integration (Luchner, 1992; p 60).

Of course, this carries certain difficulties in terms of generalisation and the uses of force in integration. However, European Union is historically unique. Firstly, its membership is made up of democratically elected nation-states who have joined through their own free will; secondly, nationalism is far more important concept in people's minds today than it was at the time of

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[1] Deutsch considers that at some time people question the size of their political community and such questioning may result in action. Integration may be achieved through peaceful or antagonistical means and ". . .political communities arise as the result of historical developments some of which have to be traced in centuries long past" (Deutsch, 1954; p 57). However, political integration is only limited by the speed that individuals learn. Simply because integration took centuries in the past it does not mean that it needs to today. Communications have changed drastically and the world is a smaller place because of this; maybe political communities should reflect these changes.

earlier integration efforts; and thirdly, it is a peaceful process. Indeed, it is a peaceful process aimed at a peaceful outcome.

The term 'process' has advantages in that the outcome of integration cannot be identified. In this context, outcome and process become indistinguishable. Consequently, it is difficult to define independent and dependent variables. "For instance, is increased economic interdependence a precondition for integration or the outcome of integration?" (ibid, p 63). It is at this point that Haas provided his analysis of the process and progression of integration in the form of spillover and supranationality (Haas, 1958).

Supranationality

The concept of supranationality is a central idea of neo-functionalism and for Haas, it constituted a means by which a political community may be realised. He defined supranationality as

> . . . neither federalism nor intimate intergovernmental co-operation, even though the institutions it employs resemble those of a federation more than the United Nations or NATO. Supranationality is a unique style of making international decisions, unique because of the nature of the participants, the context in which decisions are made and the quality of decisions produced (Haas, 1964a; p 64).

Two features of the 1992 programme in particular suggested that there might still be explanatory force in neo-functionalism: the role of the Commission as a central bureaucratic actor manipulating circumstances to further integration; and

secondly, the role played by multi-national business interests in pressurising governments to complete the internal market. . . Ironically it was politicians who in 1957 first conceived the idea of a common market, often over objections from the business community. Now the situation has been reversed; it is entrepreneurs and corporations who are keeping the pressure on politicians to transcend considerations of local and national interest (George, 1994; p 7)

Heathcote (1966) identified supranationality as ". . . an academic notion-predicted rather than experienced, and to be arrived at after a process of evolution" (p 162). Supranationality affects the process of decision-making as it evolves. Furthermore, ". . . (s)upranationality may never be realised, but the ideal has already enriched international affairs" (ibid, author's brackets). Through the actions of De Gaulle it was considered that supranationality at the European level had failed, that European institutions had failed to supplant their national counterparts. "The supranational organ of the Community, a Commission, 'proposing' to a 'disposing' Council, was in the event unable to introduce a 'new method' or style to international politics, let alone to erode the sovereignty of the surprisingly recalcitrant nation-state" (ibid p 168). The Gaullist boycott wished to weaken the position of the Commission: this it achieved and thereby obstructed the process of closer union. However, as today's position exemplifies, this only delayed the process of supranationality. As Haas points out; "In supranational systems . . . the compromise pattern involves splitting the difference between the final bargaining positions of the participants. More significantly still, supranational systems feature a bargaining process which I call upgrading common interests" (Haas, 1964a; p 65).

Haas considered that De Gaulle's vision of the changes in Europe were neither supranational nor federal but confederal. As indicated by the

> . . . former Prime Minister Debre. In Europe, legitimate power is the power which comes from national sovereignty and against this power arbitrary outside tyrannies like the so-called supranational institutions can do nothing. European unity is becoming, and will continue to become, a reality through the will of those who legitimately wield power in each of the countries which together make up Europe (Press Conference Paris 1960, cited in Haas, 1964; pp 66-67).

It was in response to such an understanding that Heathcote may have considered that: "Supranational structures may not survive into 1966 . . . but . . . the Common Market need not entirely dissolve" (Heathcote, 1966; p 168). Nation-states join international organisations for increased protection, and then use them to enhance their national power and prestige. However, eventually she concedes that the model may succeed, providing that the leading power desires it. Is this the situation with Germany today? Self-interested Member States with the support of the leading power creating spillover and increasing supranationality. The leading power, in this context, (that is, Germany) is tied closely to further integration because of its political position (or lack of power at an international level).

Both Haas and Lindberg ". . . drew attention to the distinction between power issues (high politics) and welfare issues (low politics) and argued that the latter . . . bore the potential for the collective pursuit of common interests. Over time, progress in 'low politics' would produce fundamental political

consequences" (Gehring, 1996; p 228). This of course is exactly what the realists denied; that there could ever be a shift from low politics to high politics.

Haas (1958) outlined the concept of supranationalism and condoned the pursuit of an integrated Europe through functionalist means. He did not contend that their should be a constitution or federal end. However, his language did indicate that loyalties would be transferred to a supranational government whose rules were legally binding. In this context Haas' political community is less of a prediction than it may first appear. Additionally, it is difficult to define dependent and independent variables in this context[2].

Lindberg, like Haas, does not delineate an end result or a dependent variable. His definition of integration is as follows:

> (1) The process whereby nations forgo the desire and ability to conduct foreign and key domestic policies independently of each other, seeking instead to make joint decisions or to delegate the decision-making process to new central organs; and (2) the process whereby political actors in several distinct settings are persuaded to shift their expectations and political activities to a new centre (Lindberg, 1963; p 6).

The difference between the theorists lies in the premises of their theoretical propositions. Haas based his analysis on the ECSC or sector-specific integration, whereas Lindberg concentrated on the general aspect of the EEC. Indeed, the latter approach entailed political as well as administrative mechanisms to enable decision-making to take place.

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2 A dependent variable is an identifiable outcome and neo-functionalism is unable to illustrate this for the EU. Independent variables, in the context of European integration may include, the Treaties, direct elections, the SEM, EMU etc. However, these could be defined as dependent variables themselves i.e. they are or once were identifiable outcomes.

Lindberg's modification disentangled political integration from the fate of the participating nation-states and opened neo-functionalism for a more intergovernmental perspective. While it did not rule out that political integration might lead to a 'new political community', it emphasised the possibility that it could remain in a state dominated by collective decision-making (supplemented with some delegation of power) (Gehring, 1996; p 230).

This understanding has implications on later theories that consider the EU to be a confederal entity with intergovernmentalism, transnationalism and supranationalism working in tandem (Wallace, 1983).

However, both Haas and Lindberg considered that integration was a peaceful process. Indeed, they both consider the necessity of central decision-making institutions and both leave their scale and scope open. Furthermore, they each indicate changes in the expectations and activities of the political actors. These considerations are illustrated through the dynamics of supranationality and spillover (spillover will be investigated further below).

This thesis considers that the EU may be identified as a supranational entity in evolution and that this in itself is a process of decision-making. Supranationality is greater in some areas of the EU than others. Indeed, under the first pillar (e.g. single market, agriculture fisheries and transport) supranationality is at its most formidable. Under the second pillar (common foreign and security policy) supranationality is more tenuous. However, there are instances of supranationality in terms of common foreign policy e.g. the GATT negotiations. The Treaty of Amsterdam incorporates the Schengen

Agreement (the removal of internal frontier checks and enhances co-operation between police forces and legal systems. Moreover, ". . . (a) large part of co-operation in the areas of justice and home affairs (will be) subject to Community rules: the participation of all institutions, the legal review of the European Court of Justice and the use of effective legal instruments" (EUR OP, 1997 author's brackets). The concept of supranationality is bound up with the different stages of integration the completion of the SEM was expedited by the SEA and it is in this treaty that the renewed pace of supranationality may be observed. Of course, supranationalty has been taken further in the Maastricht Treaty on European Union and it will be taken a further step again by the Treaty of Amsterdam.

Supranationality is not the antithesis of intergovernmentalism, but as Haas argued ". . . a cumulative pattern of accommodation in which the participants refrain from unconditionally vetoing and instead seek to attain agreement by means of compromises upgrading common interests" (Haas, 1964a; pp 64-66). Indeed, structurally it encompasses ". . . the existence of governmental authorities closer to the archetype of federation than any past international organisation but not yet identical with it" (Haas, 1958; p 59). What it will become is unclear; supranationality is a process rather than an end. This may be identified by the on-going accumulation of European treaties and their integrative affects. This indicates the difficulty of the dependent variable and the problem of teleology; neo-functionalism fails to posit a clear end toward which a regional system should move. Haas contended that the ". . . verbally defined single terminal conditions which we worked in the past - political community, security community, political union, federal union - are inadequate because they fore-close real-life possibilities" (Haas, 1971; p 633). Others considered the European programme as ". . . a pluralistic system in evolution from nationalism to regionalism using economic integration as a

means of promoting political unity" (Mally, 1973; pp 239-240). This thesis considers that supranationality has two levels of epistemology; on the one hand, it is material in that it is the decision-making institutions in existence at a given time; while on the other, it is part of the abstract process of integration. As Mitrany noted, we have no knowledge of what the end may encompass so why invent one?

Spillover

A second central idea to the concept of neo-functionalism is spillover. This is where integration in a sector creates its own impetus and necessitates further integration both in the same, and in other sectors. "Specifically, the term spillover describes the accretion of new powers and tasks to a central institutional structure, based on changing demands and the expectation on the part of such political actors as interest groups, political parties and bureaucracies" (Haas, cited in Kirchner, 1976; p 3). Effectively, there is an interplay between spillover and supranationality in that the ". . . establishment of supranational institutions designed to deal with functionally specific tasks will set in motion economic, social and political processes which generate pressures towards further integration" (Tranholm-Mikkelsen, 1991; p 4).

Haas asserts that perceptions of *self-interest* are the driving force in the process and that this will only be generalised ". . . if the actors, on the basis of their interest-inspired perceptions desire to adapt integrative lessons learned in one context to a new situation" (Haas, 1964; p 48). "Neo-functionalism stresses the instrumental motives of actors; it looks for the adaptability of elites in line with specialisation of roles; neo-functionalism takes self-interest for granted and relies on it for delineating actor perceptions" (Haas, 1971; p

60). Haas considers that a new central decision-making body may evolve through earlier incremental steps; he also questions whether such may be foreseen by certain individuals and used to presage their designs.

This thesis undertakes an analysis of the life insurance industry and its place within the European integration process. The SEA indicates that services are an important aspect of the harmonisation process. Much had been done in the area of goods, but little in the area of services and even less in financial services. Furthermore, life insurance is a product that needs to be regulated and the extent of regulation reveals nuances in Member State interpretations of the SEM. The three generations of insurance legislation provided the impetus for pensions' legislation and banking legislation which in turn created the need for further capital market legislation. This indicated a shift from services to capital. Once a country becomes part of the EU, the spillover effect comes into operation; if a Member State is to be part of the SEM, then it must adhere to European regulations which in themselves necessitate further legislation (for a further discussion of spillover specific to financial services see Chapter Eight).

The extent to which pressures from sectors provide a positive impetus for integration (all of which are attempting to exploit the situation to their own ends) is determined by the benefit to the sector of being involved in the integration process. It may be that the spillover process then draws another sector into the integration process if the payoff is agreeable to the sector involved. If another sector does become involved in the integration process this extends the authority of the supranational entity. Fundamentally, the supranational authority is looking for consensus and a means of upgrading the common interest (Haas 1964).

With the intensification of the integration process in Europe, the spillover process and the supranational composition of the EU are, one may posit, more identifiable than ever. Helen Wallace (1990) considers that due to the internal market programme, "It could . . . be argued that the neo-functionalist concept of spillover is now being vindicated" (p 219).

For neo-functionalism, spillover is the means by which the integration process is achieved, where co-operation in one sphere spills into another. Spillover,

> . . . refers to the specific process which originates in one functional context initially separated from other political concerns, and then expands into related activities or it becomes clear to the chief political actors that the achievement of the initial aims cannot take place without such expansion (Haas, 1958; p 523).

Legislation in one sector creates the need for legislation in other sectors and/or further legislation in different areas of the same sector if a true SEM is to be achieved. January 1 1993 was not the end but a part of the spillover process. This is what Haas labelled the ". . . expansive logic of sector integration". Spillover is not instigated through the wish for a peaceful Europe under the enthusiasm for greater welfare, but the result of ". . . swapping concessions from a variety of sectors. . . . No statesman, even if he deeply dislikes the process, can permanently isolate his nation from a commitment to unity which is only partially implemented, unless he is willing to pay the price in diminished welfare" (Haas, 1958; p 243 and pp 283-317).

However, the extent to which changing incentives created by spillover allowed an explanation for task expansion has been a point of contention for neo-functionalism. Nye (1971) argued that the functional linkage of tasks has been a less powerful mechanism than was originally believed to be the case. Whereas, Lindberg and Scheingold (1970) wished to deny that spillover led to the Common Market. However, this thesis wishes to ascertain the extent to which, in Helen Wallace's words, spillover ". . . has been vindicated".

There are two main understandings of spillover outlined in this thesis;

(a) Spillover occurs because of the impact it has on differentiated actors, including multinationals, interest groupings, the Commission and national bureaucracies. These actors form coalitions to increase EU decision-making in new sectors, in order to protect and enhance integration in sectors where agreements have already been reached.

(b) Spillover is a result of new policies on Member States which remain coherent actors in the process and continue to make crucial policy decisions in the EU. (Member States remain central actors but they are dictated to by past actions).

> Neo-functionalists, such as Haas, purport to describe the mechanism of the linkage between integration in economic and political sectors through the concept of spillover. They use the concept to describe a dynamic and more or less automatic integrative process, gradually encompassing ever more functional sectors until, the final stage, a political union is reached (Kirchner, 1976; p 2).

This thesis considers that one may identify links in one industry, the insurance industry (vertical spillover); between the legislation in the services sector i.e. between insurance, banking pensions etc. (horizontal specific neo-functional spillover); and between sectors i.e. services and capital (horizontal general neo-functional spillover). It is also recognised that an intergovernmental process of spillover is at work within European integration i.e. in the guise of the SEA and the Maastricht Treaty, and that "... spillover requires prior programmatic agreement among governments, expressed in an intergovernmental bargain. Such a bargain is clearly important in accounting for the Single European Act" (Keohane and Hoffman, 1991; p 17). This type of spillover (spillover from treaty to treaty) may be labelled intergovernmental spillover (this is indicated by definition (b) above). However, it is apparent that wider transnational processes are also providing an impetus to harmonisation and integration. In this context, the thesis contends that intergovernmental spillover is usually confined to providing the environment for further neo-functional spillover (vertical or horizontal) to take place e.g. through the SEA and the Maastricht Treaty (this is illustrated by definition (a) above. It also considers that the Member States are pushed in this direction by the very dynamics of the spillover process (see the Spillover Model, Figs 8.1, 8.2 and 8.3 pp 277-81). Fundamentally, one may posit, that there is an interaction between neo-functional and intergovernmental spillover which enhances and deepens European integration.

As it becomes more difficult to pass further directives/regulations in an area, further amendments to the treaties are needed. This was apparent with regard to the SEA and the Maastricht Treaty and, one may argue, will become even more obvious with the actuality of monetary union.

> The current ascendancy of a qualified supranational style of decision-making is shown by the way in which, thanks to the Single Act, the Council now functions. . . . The revival of a supranational style of decision-making and the strengthening of European institutions in the Single Act resulted most immediately from decisions by governments to press in their own interests, for a removal of internal economic barriers and for institutional change that would permit such a policy to be carried out (Keohane and Hoffman, 1991; pp 16-17).

At the moment, an impasse is apparent regarding pensions, taxation and capital markets because they come under the unanimity rule. However, these one may assume, will have to be overcome either just before or, more likely, following monetary union (see the Spillover Model, Figs 8.1, 8.2 and 8.3).

This thesis attempts to illustrate the process of integration in respect of one sector and argues that supranationality and spillover may be discerned in this process. This is examined through an analysis of the decision-making processes in the European Union; an understanding of the life insurance sector in Europe and where and how it designated its emphasis in the creation of the Third Life Assurance Directive. It attempts to undertake empirical research to ascertain the extent of neo-functionalism in the creation of the EU, in terms of spillover and its supranational nature (for a further discussion of spillover explicit to financial services, see Chapter Eight).

Multi-level Governance

The multi-level governance model is based on certain aspects of neo-functionalism. It considers ". . . that European integration is a polity-creating

process in which authority and policy making influence is shared across multiple levels of government sub-national, national and supranational" (Hooghe and Marks, 1997; p 22). The model recognises the central role played by Member States in the decision-making process and considers that elements of control have been passed on to supranational institutions. Consequently, in certain areas Member States have lost aspects of their sovereignty.

> In short, the multi-level governance model claims that the locus of political control has changed. Individual state sovereignty is diluted in the EU by collective decision-making among national governments and by the autonomous roles of the European parliament, the European Commission, and the European Court of Justice (ECJ) (ibid, p 22).

If the multi-level governance model is to be accepted a number of premises must hold. Initially the supranational institutions (Commission, European Parliament and ECJ) should share authority with the Council of Ministers. Secondly, that the individual Member State executives should be unable to continually stamp their authority on collective decision-making. And finally (especially in respect of this thesis) we would require that ". . . that sub-national interests mobilise directly in the European arena (ibid, p 24).

Neo-functionalism: Problems and Debate

In the 1960s and 1970s, it seemed that the neo-functionalist process of integration had lost its way. However, with the speeding up of integration during the 1980s and the 1990s, one can perceive the re-emergence of the process in certain areas of integration. Elites draw up the parameters of the

system; consumers, voters and others illustrate their preferences once the parameters have been negotiated.

Any study of integration is dogged by the problems of defining the dependent variable so that it is distinguishable from independent variables and the difficulties of concentrating on a specific region without considering external influences. The inability to overcome these difficulties in the aftermath of the Gaullist attack on European integration indicated the limitations of neo-functionalism. "Has De Gaulle killed the Common Market and with it the notion of a united Europe?" (Haas, cited in Luchner, 1992; p 66). In today's atmosphere, it is obvious that De Gaulle did not destroy European Union but he did damage the theorising about integration in general and neo-functionalism in particular (Luchner 1992). The De Gaulle incident illustrated that there were two weaknesses with neo-functionalism; firstly, that economic incrementalism was not always superior to political decisions; and secondly, the deterministic aspect of neo-functionalism was indicated. Indeed, European integration was shown not only to be an economic undertaking, but political also. Haas (1964) considered neo-functionalism to be one of the most promising methods of analysis. He posited that integration would take place in the EU and the process illustrated that, the validity of the nation-state was untenable in the post-war world. He considered that sovereignty would be gradually eroded through people's voluntary decisions or the intended and unintended consequences of such decisions, but, never by force. In this context he was deterministic. However, he does not delineate an end result; an outcome of integration.

In this thesis, there is a concentration on the European political elite and an economic elite (in this instance, the life insurance industry). As Haas identifies,

> In our scheme of integration 'elites' are the leaders of all relevant political groups who habitually participate in the making of public decisions, whether as policy-makers in government, as lobbyists or as spokesmen of political parties. They include the officials of trade associations, the spokesmen of organised labour, higher civil servants and active politicians
>
> (Haas, 1958; p 17).

Does the above illustrate the European process, can or will individuals ever learn to think in non-national terms because of technical co-operation? This investigation explores how realistic this is by undertaking an empirical analysis of the life insurance industry in the EU. Of course, we will not be able to illustrate whether a world affiliation may be realised but, we may be able to map out a transference from the national to the European which may have implications for an embryonic world citizenship.

Mitrany (1944) considered that if people are given a modicum of what they need for survival they will keep the peace. He emphasised that this has been done regularly at the national level yet it has not been tried internationally. In this context, one may identify the idea behind European integration in the post second world war period. Out of the more general international functional process grew the concept of regional integration or neo-functionalism which emphasised the evolving EU.

Integration in the EU would be brought about not simply through the efforts of politicians but through the interaction of governments, interest groups, bureaucracies and technocrats. The process would be undertaken incrementally by rational administrators rather than ideology. Individual

ideologies would be brought to the decision-making processes but these would need to be compromised in a technocratic Europe. Bureaucratic rule in the EU should not suppress political conflict but provide a better means of resolving conflicts successfully, one more apt than parliamentary democracy. Haas (1964) stressed the need for institutions whose task it would be to channel conflicts into merged ideological patterns. This concept was taken up in his later works in respect of overcoming turbulence and creating wholes (Haas, 1975; 1976).

As touched on above, there are, it has been suggested, two main limitations to the neo-functionalist approach: its confinement to Western Europe; its ability to predict. Neo-functionalists do not agree on a dependent variable and consequently differ on the extent of integration. The processes of supranationality and spillover have been indicated, but the extent to which this encompasses a regional community depends on one's concept of the dependent variable (Haas, 1971).

Ultimately, Haas denies neo-functionalism and considers it obsolescent and that European Union was linked closer to interdependence[3] than integration. Haas does not suggest that incrementalism is dead but that it had been ". . . infected with a different and more holistic decision-making rationality as the original objectives of the actors are buffeted by the condition of turbulence" (Haas, 1975; p 177).

Haas considers that if the functional and neo-functional theories are to remain relevant,

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[3] Interdependence theory like neo-functionalism contradicted the realist concept of power politics. Its premise concentrated on functional cooperation and the participation of non-state actors in the decision-making process. (For further discussion see Keohane and Nye 1972 and1974; Taylor, 1980; Gehring 1996).

> . . . two conditions must hold: (1) institutional outcomes must be open in the sense that various end states are possible, provided only that the collective decision-making mode adopted will be more centralised than was true at the beginning of the process; (2) the pressure for including common tasks and programs directed against external forces and states must not be resolved in such a manner as to detract from regional centralisation (Haas, 1975; p 178).

Through his concept of the turbulent field, Haas goes on to explain that the logic of incrementalism and regional self-containment is no longer applicable to certain areas of the EU. Turbulence identifies the ". . . confused and clashing perceptions of organisational actors which find themselves in a setting of great social complexity . . . and confusion dominates discussion and negotiation" (ibid, p 179). In such an area or ". . . space it is very difficult for organisational actors to develop stable expectations. . . . If one is not sure of one's own goals, it becomes very hard to adjust one's behaviour to the goals of negotiating partners who are no more certain of their objectives" (ibid). How far does this exist in an EU that has agreed the SEA, Maastricht, the SEM and put into operation a timetable for Economic and Monetary Union (EMU)? As Haas himself contended: ". . . if a common monetary policy is agreed as a result of the pressure for maintaining the customs union, we would have a classic case of spillover" (ibid, p 178). With the new direction the EU has acquired is it still a turbulent field? Is ". . . everything still up for grabs"? (ibid, p 179).

To overcome this, Haas considers the idea of creating wholes and initially quotes Du Gard;

I believe that though all the phenomena of life have not yet been analysed, they will be analysed one day. As for the first causes of these phenomena, I believe they lie outside our range, and no research, however thorough, can elucidate them. Owing to his limited place in the universe, man is by nature a relative and finite being, incapable of forming conceptions of the Absolute and the Infinite. He has invented names for what

> transcends himself, but these have not got him any further; he is a victim of his terminology, for those words and names do not, so far as human understanding is concerned, correspond to coginizable reality (Jean Barois, cited in Haas, 1976; p 828).

Derrida (1992) makes a similar but more specific point. "Something unique is afoot in Europe, in what is still called Europe even if we no longer know very well what or who goes by this name. Indeed, to what concept, to what real individual, to what singular entity should this name be assigned today? Who will draw up its borders? " (p 5).

Haas contends that wholes are sought to give some understanding to the world and that these are approached through system theory; he contends that the type of system theory he finds useful ". . . features the inductive method in the construction of reality and uses the perceptions and actions of concrete human beings in grappling with reality as its main data. . . . They are constructed in the sense that the theorists considers them as heuristic approximations rather than networks of determinative 'laws' constraining choice" (Haas, 1976; p 839). Whole systems or determinant variables are not cast in stone: they are ". . . not an infallible guide to international political action" (ibid, p 840). If one looks at humanity's attempt to understand itself, one will notice the short time that this has been pursued; the paradigm that

humanity sets up as a means to understand itself is only two hundred years old. "If human evolution is so recent a thing, how much more space is there to be traversed before it makes sense to think of some end state?" (ibid, p 841). In this context, why should neo-functionalism need to identify some end state to encompass a valid means of understanding aspects of European integration? The methodology used in this thesis complements Haas's comprehension of theory. Grounded theory pursues an understanding of phenomena, from the starting point of induction. Through an interaction between induction and deduction it builds a substantive theory which allows an understanding of the process of European integration without delineating an end-state or dependent variable (see Chapter Two above).

Sweeney (1984) argues that neo-functionalism does not lend itself to systematic analysis because: (1) it shifts its emphasis over time; (2) its hypotheses are developed by theorists who disagree; (3) theorists develop their own set of definitions and terminology. It is posited that neo-functionalism fails to indicate one clear end point toward which they expect a region to move. There is much debate about ends but there is no clear indication of the final goal. Schmitter (1971) identifies two levels to the dependent variable and considers ". . . whether member states will expand or contract the type of issues to be resolved jointly . . . or whether they will increase or decrease the authority for regional institutions" (p 841). Nye (1971) considers that the neo-functional approach is more appropriate in the analysis of common markets where ". . . significant institutions have been created or market forces released" (p 192).

Over the 1960s and 1970s, the concept of neo-functionalism was refined. However, it still carried difficulties indicative of its inception; criticisms that were levelled were its inability to be used in analysing the changed Europe of

the 1960s and that it was Eurocentric. It has been suggested that neo-functionalism can be modified so it may be used in a comparative framework:

> (1) the dependent variable is stated less ambiguously (2) the idea of a single path from quasi-technical tasks to political union by spillover is dropped and other potential process forces and paths are included; (3) more political actors are added; and (4) the list of integration conditions is reformulated in the light of comparative work that has been done on integration processes in less developed areas (ibid, p 193).

The problem is that the dependent variable reflects the preferences and interests of those that pursue the option. Those that perceive economic interdependence as the means of alleviating war may consider economic integration as the dependent variable; those who perceive policy co-ordination as the means of achieving this may perceive political integration as the dependent variable. Of course, within these two broad areas we have different concepts of what political and economic integration entails.

Sweeney (1984) argues that there is no clear labelling of the neo-functional goal from Schmitter, Lindberg, Nye or Haas. However, the first three attempt to revise the model whereas Haas considers the difficulties of identifying any dependent variable and contends that theoretical systems are for overcoming the very turbulence that human investigation creates. As Mitrany insists we do not know what the end result will be, so why invent one? Haas does however provide choices of outcome in the theories ". . . between federation, return to national sovereignty, and the actual situation which prevails in the European Community" (Haas, 1975a; p 175).

This thesis does not deal with scientific prediction and recognises the difficulties in identifying an end or conclusion to the European integration process. However, it does intend to put forward a number of propositions.

> While most scholars could agree to differentiate between the process and the outcome of integration, they did not agree on what this outcome should or would look like . . . Haas argued that the integration process might lead to a 'new federal organism' although the emergence of a political community need not pre-suppose the emergence of a federal state . . . Since no universally accepted dependent institutional variable could be devised, the described integration outcomes were ideal types . . . rather than scientific predictions (Luchner, 1992; pp 68-69).

This problem led some scholars to abandon the subject because it was felt that the outcome of the process needed to be explained in institutional terms. However, does this really need to be the case? Does theory always need to encompass prediction? This thesis considers that theory can be built to enhance understanding and that this may shed light on the process in relation to formal theories. "In sum, it is reasonable to agree with Haas that the search for a dependent variable and its distinction from independent variables is difficult at best and at worst futile" (ibid, p 71).

European Integration Theory: A Synergy

With the advent of the SEA, neo-functionalism once again seemed a means of explaining European integration. Even though Keohane and Hoffman (1991) considered that the EU was an ". . . experiment in pooling sovereignty, not in transferring it from states to supranational institutions" (p 277), they

also indicated that ". . . the concept of supranationality that Ernst Haas developed 20 years ago remains relevant, although it has so often been stereotyped, misinterpreted or ignored. The European community can best be viewed as a set of complex overlapping networks in which a supranational style of decision-making characterised by compromises upgrading common interests can under favourable conditions lead to the pooling of sovereignty" (ibid). However, Moravscik (1991, 1993) considered that intergovernmental institutionalism was the major dynamic in the European integration process and that this was made up of: intergovernmentalism; lowest common denominator bargaining; the protection of sovereignty; international institutionalism and domestic politics. He also argued, that ". . . the primary source of integration lies in the interests of the nation-states themselves and the relative power each brings to Brussels (ibid, 1991; p 75). Furthermore,

> Where neo-functionalism emphasises domestic technocratic consensus, liberal intergovernmentalism looks to domestic coalition struggles. Where neo-functionalism emphasises opportunities to upgrade the common interest, liberal intergovernmentalism stresses the role of relative power. Where neo-functionalism emphasises the active role of supranational officials in shaping bargaining outcomes, liberal intergovernmentalism stresses instead passive institutions and the autonomy of national leaders (ibid, 1993; p 482).

Sandholtz and Zysman (1989) and Sandholtz (1994) disputed Moravscik's and Keohane and Hoffman's understandings of European integration. However, they consider that competing ". . . explanations often represent . . . different levels of analysis. In the end it is not a matter of which one is better, but of whether the right questions are being asked" (p 127) Indeed, their paper

attempts to frame the right questions and indicate analytical links between them. They contend that in respect of European integration the process is ". . . one of bargains among nations and elites within the region (ibid). Furthermore, they consider that this effort has been ". . . guided by three groups: Community institutions, industrial elites and governments. The Commission proposes and persuades. Important business coalitions exercise indispensable influence on governments" (ibid). Unlike the early neo-functionalists, they do not consider that outcomes are determinable but ". . . dependent on the timing and dynamics of a long series of contingent decisions. But the story, and consequently the analysis, concerns political leadership in creating a common European interest and then constructing a set of bargains that embody that understanding" (ibid, p 519). Furthermore, Sandholtz (1994) considers that if decision-making was purely intergovernmental, monetary union would not have been entertained. The SEM programme ". . . produced a renaissance in pro-EC sentiment and that enthusiasm coupled with broadly supportive public and business opinion" (ibid, p 288) allowed the conditions for monetary union to be taken seriously. The 1992 programme ensured that the ". . . Commission's depiction of EMU as a necessary complement for the single market could reach a receptive EC audience" (ibid). In this context, both spillover and supranationalism were at work in the process of European integration.

The above theorists illustrate three understandings of the integration process: one that is totally intergovernmental (Moravscik, 1991; 1993); a second that illustrates both neo-functional and intergovernmental tendencies but puts more emphasis on intergovernmental processes (Keohane and Hoffman, 1990; 1991); and a third, which also illustrates both theories but puts more emphasis on neo-functional processes (Sandholtz and Zysman, 1989; Sandholtz 1994). Through an empirical analysis, this thesis reassesses these

difficulties and comes to conclusions in respect of neo-functionalism and intergovernmentalism.

Supranational Institutions (the Commission, Council, ECJ and European Parliament) and European Integration

The EU encompasses three major decision-making institutions: the Commission which initiates legislation; Parliament which gives an opinion on legislation and sometimes more (the precise role of the European Parliament in the legislative process depends on the Treaty article on which the proposed legislation is based); and the Council which adopts legislation. The European Court of Justice should also be included. (See further Chapter 5, pp 127-147 Treaties of Rome HMSO 1988). The Commission is:

> . . . appointed every four years (and) according to article 11 of the Treaty, the method of appointment must be by common accord of the governments of the member states. In practice . . . Community consciousness is neither achieved nor attempted . . . in theory the Commissioners are collectively appointed, they are in fact national nominees (Nugent, 1995; p 56, author's brackets).

Theoretically, the Council and Commission have different allegiances. The Council incorporates the most precise intergovernmental element of the EU institutional structure and was devised to ensure an intergovernmental dimension to the Union Treaties. Article 152 of the EC Treaty states that the Council may request the Commission to undertake any studies the Council considers desirable for the attainment of common objectives, and to submit to it any appropriate proposals. Some consider that the clause is over-used by the

Council and is against the spirit of the Treaty. However, the Council is an important institution and usually its wishes are followed by the Commission.

The main and initial emphasis of the Treaties is that the

> . . . Community shall have as its task . . . by establishing a common market and an economic and monetary union and by implementing the common policies or activities referred to in Articles 3 and 3a to promote throughout the Community a harmonious development of economic activities sustainable and non-inflationary growth respecting the environment, a high degree of convergence of economic performance, a high level of employment and social protection, the raising of the standard of living and quality of life, and economic and social cohesion and solidarity among Member States (Article 2, EUR OP, 1992).

The SEA added impetus to the harmonisation and integration process when it provided that ". . . the Common Market shall be progressively established during a transitional period of 12 years . . . divided into 3 stages of 4 years." (HMSO, 1988; Article 8a). And, ". . . adopt measures with the aim of progressively establishing the internal market . . . on 31st December 1992." (ibid, Article 8b). This recognised that the Common Market was not a common market at all, but because of the trade barriers i.e. administration costs, customs etc, it was no more than a glorified customs union. Consequently, it was necessary to harmonise or remove the disparate Non Tariff Barriers (NTBs) that created problems for cross-border trade. Indeed, the EU needed to face wide-scale re-regulation, which in some areas constituted deregulation. The SEA was a political means of overcoming barriers to trade.

It builds on existing policy and extends the powers of the Parliament. Its provisions included:

1. Constitutionalisation of the European Council.
2. Co-operation Procedure including Qualified Majority Voting (QMV).
3. An outline for 1992 and the following programme.

The Maastricht Treaty picks up the programme at this point, and adds:

1. Subsidiarity.
2. Single Economy.
3. Single Currency.
4. Common Policy.
5. European Citizenship.
6. Social Charter.
7. Co-decision Procedure.

In each Treaty amendment, the powers of the European Parliament are extended and the involvement of the Member States diluted. This, it may be argued, is an intensification of supranationality. Even though there is Member State input the pooling of sovereignty or the sovereignty shift is in the direction of an institution that continually broadens its remit and subsequent sovereignty.

Through the pursuit of the SEM, the EU organised a structured system of legal rules with its own sources, and its own institutions and procedures for making, interpreting and enforcing those rules. The EU Treaties have incrementally created an evolutionary legal system which, on the entry into

force of each Treaty, became an integral part of the legal system of the Member States and which their courts are bound to apply (Case 6/64 *Costa v ENEL* [1964] ECR 585, 593). At the Hague Conference in May 1948, it was held that the time had come for the nations of Europe to transfer certain sovereign rights in order henceforward to exercise those rights jointly. "The states have thus conferred on the Community institutions powers to take measures . . . thus submitting their sovereign rights to a corresponding limitation" (Case 17/67 *Newman v Hauptzollant Hof* [1967] ECR 441, 453).

The mechanisms that create legislation essentially come under two headings: regulations and directives. The Treaty defines a regulation as that which will have ". . . general application. It shall be binding in its entirety and directly applicable in all member states" (HMSO, 1988; Article 189). This was emphasised in a 1970s judgment where it was held that a regulation ". . . renders automatically inapplicable . . . any conflicting provisions of current national law - in so far as they . . . take precedence . . . in the territory of each member state" (Case 106/77 *Amministrazione delle Finanze dello Stato v Simmenthal SpA* [1978] ECR 629, 643). Indeed, it is clear, that national law is subordinate to the wording of a regulation. However, in respect of directives the Treaty provides that they shall ". . . be binding, as to the result to be achieved upon each member state to which it is directed, but shall leave to the national authorities the choice of form and method" (HMSO, 1988; Article 187 (3)).

The main difference is that a regulation is automatically imposed upon a Member State in its entirety; whilst a directive must be transposed into national law within the prescribed implementation period. Consequently, one is of an integrative nature while the other leans toward harmonisation.

However, with the mechanism of mutual recognition at some point the directive will need to become all encompassing.

Keohane and Hoffman (1991) considered that the EU had gained an element of Member State sovereignty. "Its institutions have some of the authority that we associate with institutions of sovereign governments: on certain issues individual states can no longer veto proposals before the Council; members of the Commission are independent figures rather than instructed agents" (p 278). Indeed, a number of commentators consider that European institutions have played a central role in creating the new impetus toward European integration.

> In 1984 the European Parliament submitted a draft treaty establishing the European Union, followed only a year later by the Cockfield White Paper laying out the plans for creating a genuine barrier-free internal market by the end of 1992. In 1986 an Intergovernmental conference was convened to negotiate the Single European Act (SEA). These three significant steps deeply influenced Community processes, peoples and structures and clearly transformed what was universally viewed as a sclerotic and ineffectual entity into a dynamic force in European and world affairs (Cafruny and Rosenthal, 1993; p 2).

The main debate regarding the extent of supranationality revolves around how far this dynamism was down to European or Member State influence. Moravscik (1991) contended that the supranational model emphasised the European Parliament and that ". . . government representatives, abetted by the Commission, deliberately excluded representatives of the Parliament from decisive meetings" (p 20). However, it is clear that the European

Parliament did have a role in the process and wielded much greater influence than it did on its inception. Furthermore, it gained much decision-making influence through the SEA and the Maastricht Treaty and in this context one may question the extent to which the Commission was manipulated by government representatives in the negotiations.

Spillover, Supranationality and Interest Groups: Processes of European Integration?

The EU has changed dramatically since its conception and one may consider that this has been achieved through the interaction of supranationality and spillover. European institutions have grown in their ability to initiate and pass legislation of a European nature; the European Parliament has accrued greater decision-making powers regarding European policies and has become a relevant element in the decision-making process. Indeed, spillover has been at work in respect of the supranational bodies themselves. Interest groups proliferated around the European institutions in the mid-eighties and early nineties. Why they did this is open to interpretation. However, the most obvious reason would be the affects of the SEA and decision-making procedures (qualified majority), the SEM, the Maastricht Treaty and the possible advent of EMU.

This thesis has interpreted supranationality as an abstract and material process that goes hand-in-hand with spillover; both the European Parliament and European integration allow examples of this process. The European Parliament began life as an advisory body and slowly evolved into what we have today, a democratically elected body with some decision-making powers. However, it is impossible to say what it will ultimately become in terms of its supranationalism. One may posit that it should be a decision-making

institution on behalf of the European 'citizen' and that this is its ultimate end which would link in with a federal Europe and the more general interaction (in spillover-supranational terms) that has been taking place. However, the European Parliament has accrued powers through the Treaties and intergovernmental agreements or through intergovernmental spillover. The intergovernmental aspect of the spillover process provides an environment for neo-functional spillover and neo-functional spillover provides an impetus for further intergovernmental spillover (see the Spillover Model, Figs 8.1, 8.2 and 8.3). Indeed, there is an interaction between intergovernmental and neo-functional spillover which intensifies European integration and enhances the position of the decision-making institutions and supranationality.

The process of interaction between spillover and supranationalism can be identified in the process between the Treaties, Member States and economic sectors. The Treaties have been necessary to enable a customs union and, through the SEA the foundations of a common market or the SEM. Additionally, they allow the free movement of services, labour, capital and goods and the prospect of monetary union. With the realisation of the SEA and SEM, sectors/industries recognised the increased importance of European integration and participated in the harmonisation process through lobbying both the national and the European institutions. This enhances the supranational status of the European bodies (Richardson and Mazey, 1996).

As integration intensifies, the stakes become higher; EMU, as Maastricht identifies, incorporates a European System of Central Banks (ESCB) and a European Central Bank (ECB). Eventually, the ECB will take over from the ESCB and will determine European monetary policy. The problem is of course accountability: should an unelected body have such unrestrained

power? If not, to whom or what should it be accountable? If it is accountable to the Council of Ministers, this may undermine its ability to function as a European entity in charge of a European currency. Effectively, national considerations will blur certain issues and undermine the very concept of a united economic policy. In this context, the European Parliament could extend its supranationality and become a democratic entity that makes decisions on behalf of its electorate in respect of European issues. The extent to which it attains and manipulates power will be determined by its electorate and the Member States. However, on this logic, monetary union necessitates a shift of sovereignty, in certain areas from the national to the supranational.

Much of the pro-European optimism of the 1960s with regard to European integration and union has re-emerged over the 1980s and 1990s. If we accept Lindberg's definition of political integration that

> . . . the essence of a political system . . . incorporates . . . the existence of a legitimate system for the resolution of conflict, for the making of authoritative decisions for the group as a whole (and) . . . political actors in several distinct settings are persuaded to shift their expectations and political activities to a new centre (Lindberg, 1963; p 22 author's brackets).

then a political system is in the process of formation.

In the above context, the optimism of the past is being transformed in the present to give some form to the future. Indeed, turbulence is being overcome and wholes are being created. Much has changed in terms of the environment (the EU) as the process has moved forward. The new Europe

> . . . interacts far more intensively, economically and socially; and that interaction is likely to intensify further within the next decade. But the dynamics of such integration are not peculiar to Europe: interaction within national societies and economies, within the global economy and its associated networks of social transactions and communications, respond to the same technological and economic changes (W. Wallace, 1991; p 20).

It is contended that there is more intensity to the process in Europe, but the process is a world-wide phenomenon and as this interpretation suggests, regional integration through neo-functionalism is part of international integration through functional processes.

Member States no longer have total control over all authorities in their territory, nor are they independent of outside bodies. Through the SEA, the Maastricht Treaty and the SEM, the supranationality of the EU has been intensified. It is not a federal state nor a confederation, but in the process of becoming: this it achieves through neo-functionalism. The process was intiated through the formation of the ECSC and the EEC. Its intensification has taken place through the SEA, the Maastricht Treaty, the SEM and potential monetary and political union.

In this situation, the difficulty in establishing a SEM in financial services can be seen. In the more accommodating areas, compromises have been reached. However, there are many problems to overcome with a number of Member States entrenched in normative cultural/economic existence. Consequently, there will be difficulties to overcome for many European financial institutions. The idea of a SEM in financial services is extremely appealing but each of the Member State's industries are experienced at trading in distinct

market environments and each will be loathe to give their adversaries a competitive edge by relinquishing too much of what they are accustomed to.

It could be considered that financial services legislation has reached an impasse and that without the impetus of the greater integration that the Maastricht Treaty allowed, the harmonisation process would have slowed down considerably. However, even with the Maastricht Treaty, it is now apparent that only the less problematic areas of harmonisation have been achieved in the existing phase of integration. If an SEM in financial services is to be realised, further harmonisation will be necessary. As the Treaties point out, single markets in banking and insurance are closely linked to the free movement of capital. However, to enable the free movement of capital, one may contend that a single currency is essential and until such exists, the idea of free capital movement is unrealistic. Only once monetary union has been realised can taxation and pension issues really be discussed and compromises pursued, and only in the aftermath of further treaties will the harmonisation programme be intensified. Effectively, there are two processes of spillover at work: one at a state level and one at a supranational, sector and interest group level. The former may be identified as intergovernmentalism, the latter as neo-functionalism. The latter may be broken down into three areas: general horizontal spillover (services to capital, etc); specific horizontal spillover (insurance to banking, i.e. sector bound); and vertical spillover (within insurance) (see the Spillover Model, Figs 8.1, 8.2 and 8.3). Indeed, if the impetus of spillover in relation to financial services is taken into consideration along with plans for the free movement of capital one may posit that European integration is on-going and may be unstoppable.

Neo-functionalism emphasises the role of sectors in the international economy and the extent to which a supranational authority would engender economic benefit and political acceptance of the process. Consequently, these factors add impetus to further integration in other sectors until a single economy emerges. This single economy will necessitate a single political authority and through the idea of spillover, one may argue, this will eventually be achieved.

Changes that have been influenced by the alterations in the USSR and Eastern Europe will necessitate new institutions to facilitate economic and social interactions. These will be ". . . decisively influenced by the capacity of the core institutions of West European co-operation: a structure which is gradually acquiring the stability and coherence of a political system, under the cumulative impact of internal integration and external challenges" (W. Wallace, 1990; p 21). This thesis explores whether there are supranational and spillover processes which engender European integration through grounded theory techniques and an inductive/deductive investigation of a specific industry that has become part of the process over the last twenty years: the life insurance industry.

There is undoubtedly the need to comprehend what is necessary if all participants are to understand which directions should be pursued. "This context provides for the potentially pivotal role of ideas. Shared beliefs may act as 'focal points' around which the behaviour of actors converge. Moreover, given that most agreements are likely to be incomplete . . . shared beliefs about the spirit of agreements are essential . . . Shared belief systems and focal points, however, do not always emerge without conscious efforts on

the part of interested actors" (Garrett and Weingast, 1993; p 176). This is how the SEA and the Maastricht Treaty overcame the problems of turbulence in general terms and how interest groups interact and form the basis for compromise, in more specific terms. This thesis tracks the initial uncertainty involved in the creation of the Third Life Assurance Directive and questions the extent to which ". . . institutions not only provide individuals with critical information . . . but also help construct a shared belief system that defines for the community what actions constitute co-operation and defection" (ibid). Effectively, Garret and Weingast consider that by comprehending how shared belief systems are created we can provide a means of overcoming ". . . the deficiencies of functionalist logic" (ibid p 177). They contend that to understand the process of European integration it is necessary to consider how interests and ideas are integrated. Their argument is that a Europe based simply on hedonistic *self-interest* would not sustain a process of integration. Indeed, divergent preferences undermine co-operation and act as a barrier to integration. Understanding how this barrier can be overcome requires analysis of institutions in the broadest sense: the embodiment and propagation of co-ordinated expectations about the internal market (that is, the creation of a shared belief system) (ibid). If such is created then, as Haas proposed, wholes may be created and turbulence overcome. Interest groups are capable of overcoming these barriers through communication, signals and incomplete information. They provide salience, enhance different perspectives and reduce uncertainty. "Lawmakers operate in highly uncertain electoral environments . . . interest groups offer to help. . . . They provide political intelligence about . . . preferences" (Hansen, 1991; cited in Ainsworth, 1993; p 44).

This thesis investigates the above through ascertaining the different regulatory environments that Member States considered the most

advantageous regulatory structure for themselves, and how these different preferences are compromised and a shared belief system created. Ultimately, we consider if such a process has neo-functional or intergovernmental tendencies. Additionally, it examines the extent of multi-level and state-centric models of governance in Europe. Usually the state-centric model is attributed with intergovernmental features, while the multi-level with neo-functional. However, one may posit that intergovernmentalism and neo-functionalism are not mutually exclusive and incompatible means of understanding European integration. Indeed, one may consider that they are different sides of the same coin. At the very least, intergovernmentalism must accept that the Commission and the European Parliament are important actors in the European decision-making process. "It is only by analysing the effects of institutional rules on the interactions among these institutions that one can understand the policies that are produced every day in the EU and hence the nature of the integration process itself" (Garrett and Tsebelis, 1996; p 294). Additionally, ". . . an international institution established by states may differentiate so much that sub-state and non-state actors actually begin to dominate relevant decision processes. However, this is not a suitable matter for deductively generated assumptions but an issue that should be settled by empirical investigations" (Gehring, 1996; p 252). Such an understanding negates the state-centric view and points toward a multi-level understanding of the processes. If supranationality is accepted then elements of neo-functionalism are visible. Indeed, this leads on to the main aims of the thesis, which are to:

(a) Construct a substative theory to ascertain the extent to which neo-functionalism/intergovernmentalism is in operation in the process of European integration .

(b) Create tables, matrices and models to illustrate certain assumptions that may be used to demonstrate the extent of neo-functional/intergovernmental processes. The tables, matrices and models are the building blocks of the substantive theory.

(c) Illustrate how far the EU is a supranational construct/process and the extent to which it interacts with spillover in its formulation.

(d) Provide verification of the tables, matrices and models through empirical research which includes interviews and surveys, and add to the substantive theory to allow further understanding of European integration.

(e) Illustrate clearly how the substantive theory is juxtaposed and linked to the formal theories of neo-functionalism and intergovernmentalism.

An empirical analysis that sets out to explore the above questions will be undertaken in the rest of the thesis. In the next chapter, the object is to indicate how the different legislative structures of the individual Member States provide differing regulatory environments. It is argued that regulatory environments are identifiable through individual Member State legislation and through this can be differentiated between themselves and in relation to the evolving SEM. Additionally, a survey of the EU insurance industry verifies and adds to the open coding of Member State legislation and enhances the regulation matrix. Indeed, along with with Table 2.2 (p 50) the matrix is the basis of the substantive theory.

Chapter Five

Regulation Matrix Development: Foundations of Substantive Theory[1]

You Greeks oh isn't it great to be rid of plots and battles?
Before another pestle dishes us, come let us wrestle
And pull peace out of her pit, who is so beloved by all.
You farmers, merchants, labourers,
Craftsmen, aliens, visitors . . . Come one and all to a man.
(Aristophanes, 1970; pp 233-234).

Introduction

Ellis (1994) inquired whether ". . . the Single European Market is a cohesive unit subject to a unified set of laws, or whether it is in fact, really made up of twelve separate national markets with distinct legal systems?" (p 41). The purpose of this chapter is to examine the different legislative environments and consequential regulatory regimes with regard to life insurance in the EU. However, prior to this we must classify the types of regulation which underpin the insurance law of the EU. Regulation may be classified into three constituent parts: Insurance company law; insurance intermediary law; and insurance contract law. "The aim underlying insurance company law is to protect the policyholder . . . by ensuring the finical stability of insurance companies . . . In the case of insurance intermediaries . . . protection may extend to the supervision of insurance selling practices" (Ellis, 1995; pp 46-47). Indeed, these two areas were dealt with by the Third Life Assurance Directive

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[1] In this chapter there is a comparative analysis of Member State regulations pre-third life insurance directive. It is recognised that since this analysis there have been many changes to individual Member States legislation and subsequent regulation. Indeed, this factor substantiates the author's understanding of the harmonisation processes. Each Member State has needed to bring it's regulatory environment into line with that indicated by European legislation.

whereas the area of contracts was not. A contracts directive was proposed but agreement could not be reached (the implications of this are discussed further below). Consequently, this chapter deals primarily with the implications of the first two forms of insurance regulation.

In this context, legislation underpins regulation because interpretation of the legislation creates the regulatory environments and the subsequent trading structure. In general, policy-makers find ways of overcoming conflict through negotiation and compromise. Indeed, because societies cannot be based on conflict alone, as Jordan and Richardson put it ". . . the logic of negotiation appears inevitable" (cited in Mazey and Richardson, 1996; p 201).

> This may be *especially* true in a policy-making system such as the EU where European-level officials face unique problems in formulating laws which can be made to work (and are acceptable) in . . . very different Member States. Each of these states has different regulatory styles and traditions and it is an exceptionally difficult task to produce proposals which can mobilise the necessary winning coalition. . . . One way of doing this it to integrate interest groups directly into the various stages of the policy process from problem identification through to policy implementation (ibid).

Through a comparative analysis of Member State legislation in respect of the life insurance industry, theoretical coding (see Chapter Two) and a survey of European life insurance companies, a regulation matrix is constructed that pursues further understanding of the European integration process and the extent of state interference in Member State life insurance markets. Such will

establish the underpinnings of a substantive theory which will be developed further in the following two chapters.

The initial questions that need to be asked when one broaches the subject of regulation in the EU are: what are regulations, how would one define them and how do regulations and the EU fit together? Additionally, the concepts need to be understood in their historical context, with regard to their theoretical underpinnings and their more practical applications.

First, the chapter will give a brief definition of regulation. Secondly, it builds on Table 2.2 and further defines what a regulatory environment entails. Each Member State's life insurance industry undergoes comparative analysis and is coded in a regulation type category. The 12 (pre-enlargement) Member State life insurance industries are then pin-pointed on a regulatory environment matrix (see the Life Insurance Regulation Matrix One, Fig 5.1 p 157). This displays the amount of regulation on a scale of 1-12. Each unit of the matrix indicates the regulatory regime of the given Member State and displays the type of legislation that indicates the regulatory environment.

Thirdly, a survey (via a postal questionnaire) of European life insurance companies in eight Member States is added to the existing coding. Indeed, this verifies the matrix and creates a more precise understanding of the area under analysis. This is illustrated through the augmented matrix (see the Life Insurance Regulation Matrix Two, fig 5.2 p 160). Indeed, the coding process takes into consideration the legislative positions of the Member States and in the case of eight Member States allows individuals from separate life insurance sectors to contribute their own perceptions of the legislation that underpins their regulatory environments. The regulation matrix is intended

to reflect the Member States' regulatory positions during 1993-94 i.e. prior to enlargement and the enactment of the Third Life Assurance Directive.

In the questionnaire, respondents were also asked to indicate which type of life insurance regulatory environment prevailed in their own Member State and what type would be most advantageous (a) for their own company, (b) for the European Union (c) to allow greatest consumer protection, and (d) to enable greatest consumer choice. The results added to the coding and categorisation process, assist in identifying a compromise convergence point and allow some verification of the pre-suppositions accrued through the comparative analysis of the Member State regulatory environments. (The methods and methodology were illustrated in greater depth in Chapter Two)

Regulation: A Definition

Regulation has a multitude of definitions. However, for the purposes of this thesis it shall be considered as ". . . a politico-economic concept and, as such, can best be understood by reference to different systems of economic organisation and the legal forms which maintain them" (Majone, 1990; pp 1-2). Regulation is an attempt to correct market failure in the form of ". . . monopoly power, negative externalities, failures of information, or insufficient provision of public goods such as law and order or environmental protection" (Majone, 1996; p 263). Furthermore ". . . market activities can be regulated only in societies that consider such activities worthwhile in themselves and hence in need of protection as well as control" (ibid).

Additionally, it may be argued that, there is a delineation between social and economic regulation. Social regulation ". . . deals with such matters as health

and safety, environmental protection and consumer protection" (Ogus, 1994; p 4). Some regulatory regimes are of a liberal nature whereas others are state-controlled and have been allowed a modicum of monopoly or oligopoly.

Regulation can be traced back to the Tudor and Stuart periods, e.g. through guilds. However, by the late nineteenth century, this tradition had largely disappeared and regulation emerged in coincidence with industrialisation and urbanisation. Dicey (1962) considered that the growth of regulation illustrated a collective disenchantment with *laissez-faire* that was fuelled by the expansion of suffrage. However, on this there has been disagreement and some consider that there ". . . never was an age of *laissez-faire*, and state intervention did not result from any abrupt shift to collectivist ideology but rather emerged gradually, throughout the nineteenth century, as a pragmatic response to social problems: England stumbled into the modern administrative State without design" (Ogus, 1994; p 7).

Twentieth century Europe saw an immense growth in the use of regulation resulting from Keynesian ideas and the transferral to nationalised utilities. Such encompassed a shift in economic regulation toward the social in terms of government direction and political accountability. Additionally, over the last fifteen years we have witnessed a process of deregulation or, as some would argue, a process of re-regulation. "Many so called deregulating measures have involved not the removal of external constraints but rather a change to less interventionist methods and forms . . . Some areas of social regulation have continued to grow, notably those pertaining to the environment and financial services" (ibid, p 10).

Finally, the evolutionary process toward the SEM and its impact on regulatory frameworks need to be taken into account. Different regimes create

barriers to trade. Consequently, harmonisation of regulations was posited. However, harmonisation proved a lengthy business and through the SEA, which initiated Qualified Majority Voting (QMV), and mutual recognition the whole process was speeded up[2].

Industrial societies generally accentuate a tension between two systems of economic organisation: the market system and the collectivist system. The former is where individuals and sectors are allowed to function with minimal interference in the pursuit of their own goals whereas the latter looks to control and direct behaviour through intervention. Of course, there are gradients of these perspectives in the EU, each Member State illustrating its own cultural tradition in the legislation and regulation they adhere to.

As noted above this thesis takes into consideration the special nature of life insurance and other financial services products. Indeed, the thesis posits that products such as life insurance and pensions are closely linked to individual cultures. "Differences in the way distinct countries subjectively value insurance products have not come into being by chance. They have evolved out of historical developed differences in values between one national society and another" (Hofstede, 1995; p 423). This situation exists between the separate Member States and relates to other financial services products. It is from this starting point that it is assumed that through a study of the life

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2 *Mutual recognition* is a ruling by the ECJ which states that if a product meets the stipulated standards in their home Member State then it may be sold anywhere in the Union. Mutual recognition encapsulates an important mechanism in the pursuit of the SEM as it gives a framework for the enablement of compromise. However, where diversity is so great, there will be a need for greater rather than less harmonisation of Member State legislation. The principle of mutual recognition . . . pre-supposes agreement on a number of basic rules . . . these minimum harmonisation requirements . . . are only possible because common interest, mutual confidence and a high degree of economic convergence exist between EEC member states (Loheac, 1991; p 409). One has to question if "minimum harmonisation requirements" have been met in respect of the life insurance market. The achievement of such requirements is extremely rare and even if there is a "high degree of economic convergence" in the life insurance market, the practical realities of achieving an SEM through *mutual recognition* alone are apparent. A convergence process must be undertaken prior to the actions of *mutual recognition* coming into play (ibid). The idea behind *mutual recognition* suggests spontaneous legislative adaptation; however, it does not deal with all regulation and as a convergence point is necessary for it to be effective it could be conceived as an impetus that encourages legislative change and compromise. This convergence point is indicated in (Figure 5.1 and 5.2)

insurance industry generalisations concerning the EU may take place. Furthermore, the thesis uses a qualitative methodology and generalises from one situation to others (this is made clearer in Chapter Two above and through the use of the Spillover Model see pp 277-81). In this chapter there is a comparative analysis of Member State regulation regarding life insurance and it is suggested that the conclusions may be used to understand regulatory convergence to financial services in general.

Coding and Categorisation: Member State Life Insurance Industries

"Numerous alternative economic rules could have been used as the basis for EC trade liberalisation, from pure *laissez-faire* to the creation of an encompassing set of EC regulations and standards" (Garret and Weingast, 1993; p 177). This chapter defines these alternatives and indicates their existence through theoretical coding, a comparative analysis, a survey and the creation of a regulation matrix.

Following the initial comparative analysis of the Member States life insurance legislative environments and regulatory structures, they were coded into three categories each designated the preferred type of legislation which indicated their regulatory regimes. These were: (a) liberal, (b) prescribed and (c) nationalised (state-controlled) (the initial coding is illustrated in Table 2.1 p 43).

Through the open coding, each Member State was allocated a position on the matrix between *one* and *twelve*. A perfectly free market would be at point one on the scale, while a state-controlled market would be at point twelve. This is not to say that there are no differentiation's within each market type, as

Tables 2.2 and 5.1 display, but it does allow a general means of defining different regulatory environments.

Table. 5.1

Regulation Scale

1-2 = self-minimal regulation

3-4 = minimal regulation; independent regulatory bodies

5-6 = moderately regulated without state ownership

7-8 = highly regulated without state ownership

9-10 = highly regulated with minimal state ownership

11-12 = highly regulated with a profusion of state control.

Initial open coding (see Chapter Two) allowed a comparative analysis of the regulatory environments of the individual Member States and to illustrate the process involved in the pursuit of a single market in relation to the normative perceptions of legislation and market norms. Each state has a different cultural tradition in relation to financial institutions and investment. These are illustrated through historical attitudes and economic ideologies which in turn are exemplified through legislation and the subsequent regulation relating to life insurance. Basically, through this coding the research is identifying particular phenomena in the data and grouping concepts around them. This reduces the number of units with which the research needs to work. "The process of grouping concepts that seem to pertain to the same phenomenon is called categorising" (Strauss and Corbin, 1990; p 65) (see Table 2.1).

> Once our attention is fixed on a category, we begin to examine and discover emergent properties about the category by constantly coding and analysing. Such categories and properties only conceptualise what we see, but with the theoretical codes we form the connections between them which yield hypotheses- which in turn suggests how the incidents and categories thereof may be related to each other (Glaser, 1992; p 39).

Liberal Regulatory Environments

A liberal regulatory environment lies between one and four on the twelve point scale and is characterised by the basic premise of self-regulation with minimal legislation. Four EU life insurance industries are identified as having relatively liberal environments in respect of their legislation and subsequent regulations. They are Eire, Luxembourg, the Netherlands and the UK. These life insurance regulatory structures are perceived as relatively liberal in comparison with other EU Member States. However, one may consider that the Irish system, although until 1936 extremely free, is close to the prescribed regulatory environment. Neither the UK, Luxembourg, nor the Netherlands are disposed to regulations which demand governmental approval with regard to policy design or premium rates, and traditionally the Irish regulation was left in the hands of an actuary, though in 1984 financial tests were implemented in Eire.

The UK industry was supervised primarily through the Department of Trade and Industry (DTI) with regard to solvency control which relied on the principle of 'freedom with disclosure'. In general ". . . insurers are free to compete as they choose in the marketplace, provided that they meet certain requirements designed to ensure the continuing solvency of all entities

underwriting policies of insurance" (Financial Times, 1992; p 291). However, following membership of the EU and a number of company failures, the regulatory framework was intensified ". . . partly through the perceived need to protect policy-holders . . . and partly as a result of changes arising from the implementation of European Community directives" (ibid). The minimum valuation of liabilities has been delineated by a supervisor and the life office 'freedom with disclosure' allowed the actuary relative liberty to initiate: reserve calculations; premium calculations; product design; investment choice with regard to reserves. The actuary is, however, statutory bound to ensure office solvency and meet minimum reserve levels and asset cover.

Fundamentally, prior to 1936,

> . . . the general character and operation of the Irish market resembled that of the UK . . . In 1936, however, the Irish insurance market became protected so far as entry was concerned . . . an insurance company would not be granted a licence. In Ireland there are technical reserves, minimum solvency and guarantee funds for life insurers. However, the regulatory authority has the power to take action if the solvency level of a life company is endangered (ibid, p 153).

The Irish regulatory environment is not as free as the other liberal environments. This is due to the process of Europeanisation that has been apparent in this market. The Irish market has brought in, to a far greater extent than the UK, the European Union's (Life Insurance) regulations on top of the EU Minimum Solvency Margin Directive (1979) and therefore one may argue that it borders the prescribed regulatory environment.

Traditionally the minister left detailed financial control of authorised life insurers in the hands of the company actuary. Here again, the European influence has brought about change through the introduction of three financial tests: technical and mathematical reserves, minimum solvency margin and certification of returns for all life insurers (ibid, p 156).

However, ultimately it was judged that the Irish life market was not prescribed because life insurance company returns are completed and submitted to the ministry which, as with the UK and Dutch regulatory environments, ensured solvency margin requirements.

Luxembourg also adhered to EU legislation and its legislation of 1984 incorporated two Directives; the Co-insurance Directive 78/473[3] and Life Assurance Directive 79/267[4]. However, it is primarily concerned with the separation of life and non-life insurance with only a passing interest in solvency margins.

One may consider that Luxembourg regulation was the most liberal in Europe as neither policy wording nor rates were open to supervision. Luxembourg mainly relies on the industry itself to undertake supervision and where problems arise, the Officer of the Commissioner for Insurance (OCI) is consulted. However, the OCI does have some power and can force insurance companies to comply with Article 18 of Insurance legislation (24 Feb 1984) and may ultimately withdraw approval. This legislation ". . . modified existing legislation in order to bring it into line with existing EU directives" (ibid p 202) (Co-insurance Directive and the First Life Assurance Directive). It was

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[3] OJ L 151 07/06/78

[4] OJ L 063 13/03/79

considered that the first of these enabled EU risks to be covered through a lead insurer by a number of Member States.

> Since it is the lead insurer who agrees the premium rate and conditions, the State (Member State) of the risk would have been able to use the mechanisms applied to insurers established in its territory to ensure that the insurance product contained in the co-insurance contract matched in every way what locally established insurers provided. The participation of insurers from other states would thus have no effect, from the customer's point of view, apart from making it easier to find direct cover (without recourse to reinsurance) for large risks (Pool, 1990; p 39 author's brackets).

Fundamentally, Luxembourg companies are closely monitored and must adhere to Article 4.1 of the 1984 legislation which states that ". . . undertakings shall not be granted approval unless they assume one of the following forms: limited company, company limited by shares, mutual insurance association, or co-operative society" (Financial Times, 1992; p 204). Even the liberal markets adhere to some form of regulation. However, in the case of Luxembourg it is minimal in respect of life insurance and external companies are taking advantage of this factor. "The market . . . is liberally regulated with little involvement in the supervision of policy wordings or rates . . . Supervision is based on firm principles but exercised in a flexible way, minimising unnecessary bureaucracy" (ibid).

The Dutch industry is supervised by an independent agency called the Verzekeringskamer (VK), and companies report to this agency which enables governmental control over investment regulations and solvency margins.

Each of the Member States' regulatory systems rely on some reporting to the regulatory body.

Supervision in all four liberal regulatory environments is based on the concept of self control, self-regulation and self-determination in respect of both products and premiums. This is interposed by a regulatory structure of minimal prescription, which mainly determines insolvency regulations and supervisory bodies. With regard to the Netherlands the main legislation over the last 70 years has been 'Wet op Levensverzekering-bedrijf' (WOL) established in 1922 in the wake of two company insolvency's. This legislation was superseded in 1987 by the 'Wet Toezicht Verzekerings-bedrijf' (WTV) which monitors company insolvency margins through VK supervision and brought Dutch legislation into line with that of the EU. This indicates that European legislation affects the national and consequently impinges on the normative experience of the Member State. Such is also clear within the Irish market where all of the most recent legislation has attempted to bring it in line with that of the EU.

In the Netherlands, supervision

> . . . is of a predominantly liberal character, with the emphasis on retro-active financial supervision. The insurance company can therefore in principle determine its own company strategy (such as premiums and conditions) in accordance with its own opinion within the limits and rules laid down in the law. . . . The liberal supervision appears to protect the insured public adequately, and is efficient from an economic point of view, in that most Dutch insurance products are generally priced lower

than in other European countries which operate stricter supervision (ibid, p 213).

In the UK, the Insurance Companies Act (1982) and the Insurance Companies Accounts and Statements Regulations (1983), ensures publications of balance sheets, a life fund account and annual valuations. The Policy-holders Protection Act (1975) as amended by the Policyholders Protection Act (1997), determines that in the event of insolvency a fund is available, paid into by the industry as a whole, which covers 90% of policy-holder losses.

The Financial Services Act (1986) initiated trading supervision through the Life Assurance and Unit Trusts Regulatory Organisation (LAUTRO) and the Financial Intermediaries Managers and Brokers Association (FIMBRA). The Financial Services Act polarised agents into two categories; independent brokers were tied to FIMBRA and company representatives who sell only the products of a certain company to LAUTRO. The Act ensured that independents follow certain regulations which include detailed record keeping, disclosure of commission and best advice (this may be described as an undertaking by the broker to ensure that the proposed investment meets the customer's needs at least to the extent that any other product may). However although these bodies are independent in name, they are effectively tied to the insurance business. This has been illustrated by the shift toward a body with greater independence, the PIA. Of course, this has recently been surpassed by the Labour party's plan for a regulatory body which will oversee the whole of the sector; the Financial Services Authority (FSA) Indeed, through these provisions, one could argue that the UK is shifting towards the Belgian model.

Adherence to such regulations proved to be expensive and to cut costs, many small and medium independents tied themselves to insurance companies. Many banks and building societies have also given up their independent status, although many banks have moved further into the life and pensions market by initiating their own subsidiary life offices. Consequently, there was an element of co-operation between banks and insurance companies in the UK market, although this was tainted or slanted with a growing propensity towards competition.

Although there are similarities between these four Member States in that they each fall into the liberal category, there are also differences between them. As it is generally agreed that a totally free market is an abstract notion (as some form of regulation is always apparent), none of the Member States can be given a number one on the matrix scale (see Life Insurance Regulation Table 2.1, p 43 and Fig 5.1, p 157). Consequently, the most liberal market (Luxembourg) is at point two. Luxembourg is totally self-regulated. However, when problems do arise, the Officer of the Commissioner for Insurance (OCI) is consulted under its general insurance legislation. In considering the Luxembourg situation, one must be aware of the small size of the market and the ease with which it may be monitored.

The UK and the Netherlands have very similar regulatory environments and both may be positioned at point three (see Table 2.1 and Fig 5.1). As indicated above, the UK predominantly relied on 'freedom with disclosure' which allowed an actuary the discretion to initiate reserve calculations; premium calculations; and investment choices regarding reserves. The actuary was, however, obliged to report this information to the Department of Trade and Industry (DTI) and is statutorily bound to ensure solvency levels, minimum

reserve levels and asset cover. Of course, as indicated above, this is in the process of change.

The Dutch life insurance industry was also supervised through a regulatory body which, although independent, was still sympathetic toward the industry and is mainly concerned with minimal supervision of insolvency regulations. Legislation is minimal, however the most recent brings it into line with general European legislation.

The Irish environment was the most closely regulated in the liberal category and borders that of the prescribed. Traditionally, Irish supervision (which corresponds with the number four on the table and matrix) was left in the hands of an actuary (see Life Insurance Regulation Matrix One, Fig 5.1, p 157 and Table 2.1, p 43). However, it has tighter regulations today and is more closely in line with EU legislation than any of the liberal markets. In Eire, there are required technical reserves, minimum solvency delineation's and guarantee funds. Ultimately, the authorities can take action if the solvency level is threatened.

Therefore, liberal regulatory environments are similar in respect of ideology i.e. they have a free market ethos and limited legislation. However, despite these similarities each market has distinct differences. It could be argued that the reason for this lies in the regulation which has been defined by Member State legislation. One may consider that the differences relate to a cultural existence that is manifest in the economic sphere through definite legislation, regulation and institutional norms. The differences between the Member States in this area do, however, seem to be diminishing, as the European legal system becomes more apparent. All four above Member States have had to

bring themselves into line with EU legislation which, for them, means moving towards greater rather than less regulation.

Prescribed Regulatory Environments

This section provides an explanation and codification of what may be described as prescribed regulatory environments. Germany is the Member State with the most prescriptive regulation whereas Spain and Denmark have a little less; Belgium leans further in the direction of the liberal. Indeed, one may consider Belgium as a compromise between the liberal and prescribed regulatory environment types and one which could typify future European regulation.

A prescribed regulatory environment lies between five and eight on the scale and within this range one is looking at moderate to tight legislation but without or with limited state interference in the companies themselves. The comparative analysis and open coding has identified four Member States with lesser or greater degrees of prescription and identified their position on the matrix. They are Belgium, point five on the scale, Spain and Denmark, point six, and Germany, point eight. One may argue, that through its legislative programme the French regulatory environment falls into this category. However, at the time of the study, it still had a preponderance of state ownership and will be treated as a nationalised regulatory environment.

In the past the Belgian environment has had liberal life insurance regulation and until 1930 supervision of the system was not contemplated. However, in general, the regulatory environment has been indicative of the state of play at the European level because in the post-war period the Belgian structure evolved in line with EU directives.

The Spanish regulatory environment is similar to that of Belgium, although it does have its own distinct historical route. Until the death of Franco in the mid-seventies and the implementation of the new Spanish constitution in 1978, insurance was supervised by legislation passed in 1912. Indeed, it was not until the Socialist party attempted a reformation of the regulatory system in the early 1980s that any real legislation was formalised. The Insurance Control and Supervision Act, (Ley de Ordenación del Seguro Privado) was implemented in 1984 and with a royal decree in 1985 formed the basis of control and supervision in the Spanish market. This legislation looked towards a number of changes in Spanish regulations; these included solvency fields, policy-holder protection, professional standards and the re-grouping of companies through mergers. Supervision in Spain is straightforward: companies apply to operate in the market then seek registration. Once registered, companies are monitored in respect of solvency, advertising and products, etc by the Dirección General de Seguro which reports directly to the ministry.

In Germany, life insurance is tightly controlled and companies have to seek approval with regard to product design and policy terms. There are two main pieces of legislation which relate to insurance. These are Versicherungsvertragsgesetz (VVG), which relates to regulating the relationships between insurance companies, the insured, policy-holders and beneficiaries; and the Versicherungsaufssichtsgesetz (VAG) which is directly responsible for the regulations relating to the supervisory body Bundesaufsichtsamt fur das Versicherungswesen (BAV). "The underlying principle of the insurance supervisory law is the system of 'substantive state supervision' (materielle Staatsaufsicht)" (Financial Times, 1992; p 103). Within this framework ". . . the operations of an insurance company are

controlled legally, economically and financially from the beginning of its activities to the end of its winding up procedure" (ibid).

The BAV designates premium rates, a specified mortality table for each product, and maximum interest rates and expenses. Such a situation induces a small differentiation in the prices of products and leads to limited competition regarding product range. Because most companies have a complete product range, competition emanates from bonus distribution. Between 95% and 98% of profit is distributed to the policy-holders. A general regulation indicated that 90% of total profit should be distributed, but competition forced bonuses up.

In Belgium, supervision was extended in 1975 and all insurance was brought under the auspices of the Office De Controle des Assurance (OCA). The OCA is monitored by the Minister for Economic Affairs. However, the process is undertaken through a committee which interacts with the ministry and indicates necessary changes in respect of legislation and how it should be administered. The committee consists of six members who are drawn not only from insurance but other areas: the legal profession, other financial institutions and academia. As many areas as is possible are taken into consideration; consequently, profitability is not the only benchmark, but it is an important consideration. Indeed, the OCA undertakes the close supervision of existing regulations. It does not determine policy rates, it simply ensures that legislation is activated and adhered to through three main areas:

(1) Technical Supervision.

(2) Legal supervision of compliance with regulations.

(3) Financial supervision.

One may contend that the Belgian method displayed a consultative (and more democratic) dimension and one that gives an indication of how legislative decisions and supervision may be conducted in the future. Indeed, as noted above, the Belgian approach may display the traits of the evolving SEM in life insurance and illustrate an attainable compromise between the different life insurance regulatory environments.

Denmark was supervised through a legislative framework which established a number of acts. These include the Insurance Companies Act (1981) which prescribes public supervision and company format; the Business Competition Act (1989), which supervised monopoly and price control; the Insurance Contracts Act (1930), which concerns relationships between insurance parties, i.e. each other and customers; the Marketing Act (1975) under which the ombudsman may adjudicate whether insurance company marketing activities are in line with accepted practices. To ensure adherence to legislation and compliance with law 127 (3) the industry is supervised by a division of the Danish Ministry of Finances.

As mentioned above, the Spanish life insurance industry was supervised by the Dirección General de Seguros, an insurance board directly responsible to the Ministry of Finances. Spain has recently developed the fastest growing life insurance industry in premium income terms in recent years indicating the largest growth rate in the EU. In the latter part of the 1980s, this was as high as 70% (Sigma, Swiss Re; 4/90 - 1/92). The reason for this growth was the social security crisis which has prompted individuals to arrange their own pensions and subsequently improved sales.

In Belgium, formal approval regarding conditions and rates was abandoned and the principles in relation to insurance governance reformed. Belgian legislation was specific in content but it allowed general applications in respect of product by product profitability and the process of contractual obligations in individual cases. Effectively, supervision was non-systematic and allowed for both prudence as well as profitability. Consequently, both company and consumer needs were dealt with through the existing legislation. The Danish regulatory environment was a little more prescribed in respect of this and Danish companies submit detailed financial statements which include annual accounts and group reports. However, in respect of solvency margins, technical reserves and capital adequacy, legislation was denoted by EU directives.

The Danish life insurance market was not as liberal as its non-life insurance market and this illustrates the limited onus the Danes put on EU legislation to indicate their regulatory structure. There are more comprehensive directives in respect of non-life insurance which the Danish have subsequently implemented.

The German environment was highly regulated. This ensured high consumer protection and safe but low-yielding products. Historically, Germany has undergone two periods of hyper-inflation. This may have much to do with a risk-averse attitude and the factor of limited product innovation. Once again, the prevailing legislation and consequent regulatory structure was indicated by cultural and socio-historical circumstances.

As with the liberal regulatory environments, the prescribed environments illustrate the changes that EU legislation is bringing about with extreme clarity. The lesser prescribed markets have the fewest changes to make and

this is apparent in their adroitness at bringing in European directives. This was particularly so of Belgium. However, in this respect this it was followed closely by both Spain and Denmark. Until 1990 a life insurance company in the Danish Market was state controlled. As EU legislation changed, so too did the Danish market. Consequently, an interaction is apparent between national legislation, European legislation and regulation formulation.

The Danish market was marginally tighter than the Belgian with respect to legislation and has consequently been allocated point six on the scale (see Life Insurance Regulation, Matrix One Fig 5.1 p 157 and Table 2.1 p 43). In the Belgian (point 5 on the scale) market, supervision was non-systematic and negotiation was apparent, whereas, the Danish market called for detailed financial statements i.e. annual accounts and group reports. However, in respect of solvency margins, technical reserves and capital adequacy legislation, Denmark and Belgium were very similar as both provided extensively for EU Directives.

Spain has undergone a legislative transformation since the late 1970s and this brought about many changes in life insurance regulations. Changes have included the introduction of solvency fields, policy holder protection, and professional standards. Effectively, the Spanish regulatory environment was very similar to the Danish and was consequently, also given a six on the scale (see Life Insurance Regulation Matrix One, Fig 5.1 and Table 2.1).

Within the prescribed market environments there are differing amounts of prescription in that some border on the liberal and others on the nationalised. Germany is the most prescribed (point seven/eight on the scale), whereas in Spain and Denmark, (point six on the scale) although regulation is tight, more flexibility is allowed. As mentioned above, Belgian regulation (point

five on the scale) indicated most succinctly the impending single market environment in respect of its existing legislation. What was apparent was the consultative nature of Belgian supervision and how this did not negate but was indicative of EU guide-lines. As with the liberal environments, a convergence procedure can be detected with regard to EU legislation and consequent regulatory requirements.

Nationalised (State-Controlled) Regulatory Environments.

The nationalised or state controlled regulatory environments were placed between nine and twelve on the scale; and the open coding process placed four Member States in this category. These are France, Italy, Portugal and Greece. At the time of the study, each had a state-controlled element to its life insurance market in that there was a preponderance (45-50%) of state ownership in respect of life insurance companies.

In France, nationalisation was a post-war phenomenon, while in Portugal nationalisation did not occur until 1974. The Greek market had not been formally nationalised, but the market was state-controlled. Within the matrix the Member State markets are defined in respect of legislation on the one hand and the percentage of the market controlled by state run companies on the other. Thus, France is at point nine Italy, at point ten and Greece and Portugal at point eleven (see Life Insurance Regulation Matrix One, Fig 5.1 and Table 2.1).

In France, regulation was extensive. However, this was changing continually. "French insurers used to be seen as . . . hidebound by regulatory red tape of the former all powerful Direction des Assurances . . . this over simplified

view is now dating rapidly" (Financial Times, 1992; p 81). The principles of state-control were laid down by statute in the 1930s and

> . . . pertain both to contractual obligations and to the financial structure of the companies. As regards the legal status of insurance contracts, the controlling authority (until July 1991 the Direction des Assurances) had wide prerogatives, from the drafting of the legislation to the enforcement of compliance by the companies. . . An important aspect of this control was the obligation of insurers to obtain official approval for all new products or types of contract. The controlling authority also regulates and watches over the financial and prudential requirements (equity, computation of reserves and investment strategy) prescribed by the Code des Assurances (ibid, p 87).

The Greek and Italian life insurance industries were state-controlled in that state-owned companies exist in the market and enjoy certain benefits because of this. In Greece, 45% of the market was controlled by eight state controlled insurance companies (Financial Times, 1992). "The Greek market has traditionally been highly regulated . . . this situation is in large part a legacy of heavy government control . . . [which has] led to administrative rigidity and as a consequence high operating costs" (ibid, p 143).

In Italy, insurance companies surrendered a percentage of their business to the state controlled Instituto Nazionale delle Assicurazioni (INA). Following 1 April 1987, life companies writing life business for less than 6 years give 30% of new business, for 6-10 years, 20% and for over 10 years, 10%. This led to unfair competition in the market and allowed the evolution and maintenance of a dominant position (Munich Re, 1988). The Italian market

was supervised by the Instituto per la Vigilanza sull Assicurazioni Private de Interesse Collectivo (ISVAP). This was set up by the Ministry of Industry and Commerce and gives approval to insurance matters on its findings. There was no legislation in respect of this but the process was universally accepted by the market.

Each Member State was highly regulated (even though Italian regulation is not legislated, it is universally accepted). However, each Member State was becoming less regulated as EU legislation dictated. In Portugal, the position was that 51% of the sector remained in the hands of the state and 33% in France (Munich Re, 1988). In all cases, the state-controlled institutions were the largest in the Member State life insurance markets.

Regulation in France was supervised by the 'Direction des Assurance' which was set up by the Ministry of Economy. Rules were strict with regard to individual life insurance business. Approval was needed for product design, premiums and policy conditions. However, changes were underway to alleviate these restrictions. There was also much consultation with regard to regulation changes, and prior to any changes the 'Conseil National des Assurance' (made up of representatives of the insurance industry and authorities) was referred to. There is also a powerful consumer lobby in France which was also consulted.

The Portuguese environment was supervised by the 'Instituto de Seguros de Portugal' (ISP). This was founded in 1982 and consequently initiated the 'Plano da Explarocao' in 1985 this outlined a standard basis for life offices. The ISP exercised complete control over the life insurance market; approval for product design, premium rates, and policy wording had to be applied for and quarterly returns inclusive of profit projections had to be submitted to it by all

life insurance offices. This, one may argue, was a market in which a company was open to total scrutiny. Since June 1988 there has been greater liberty regarding expenses although the ISP still determined the mortality base, and the technical interest rate. However, it was expected that because of extended freedoms with regard to non-life tariffs these would follow in the life insurance market. "The insurance market is tightly controlled by government regulation. All insurance businesses must be approved by the Portugese Ministry of Finance" (Financial Times, 1992; p 232). The latter consults with the ISP prior to any approval

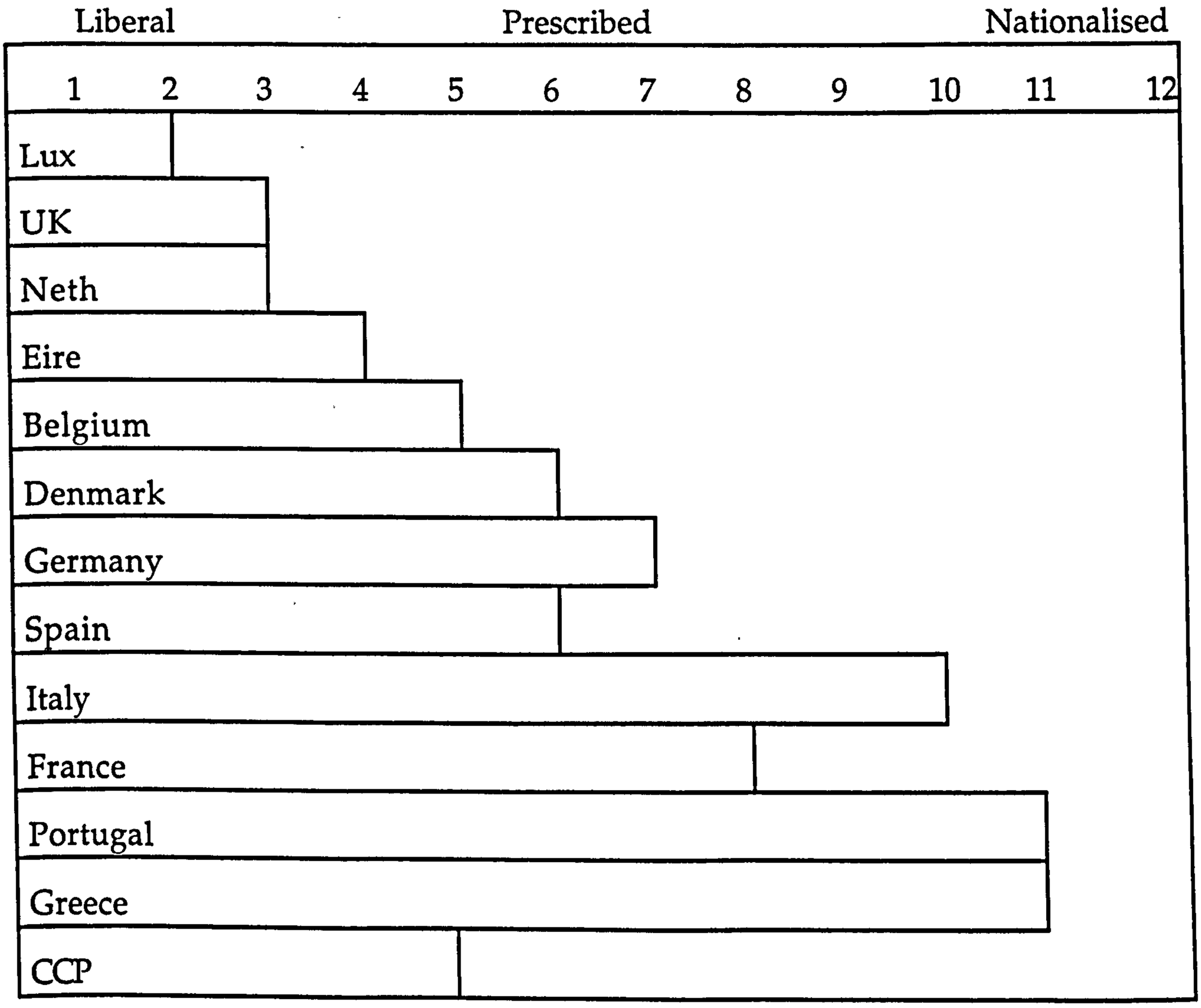
All four state-controlled life insurance regulatory environments were moving towards a more liberal trading structure (even though in certain areas of certain Member States, the markets had to be pushed). Each recognised the changes needed to facilitate competition in the single market while EU directives attempt to harmonise supervision in the direction of free market trading. The French environment could be described as the weakest nationalised regulatory structure. This could be illustrated by the failure of the French government's attempt to force a merger between two insurance companies where market benefit was not discerned by the companies involved. But it succeeded in relation to a bank and insurance company merger where market benefit was recognised. Greek life insurance, as with the financial sector as a whole, was highly regulated. One may consider that this is the legacy of heavy control in the immediate post-war period. However, regulation is slowly being liberalised to comply with EU legislation usually following European Commission insistence.

In both France and Portugal, the banking sector had recognised its potential with regard to distribution. This was especially so in France where the market was more developed. These distribution channels have been mainly used in

rural areas and as Portugal is mainly a peasant-based society they could be used to penetrate this market. In Greece, the insurance sector was dominated by the banks which were in turn controlled by the state.

Fig 5.1

Life Insurance Regulation Matrix One



CCP = Compromised Convergence Point

Matrix compiled from an analysis of Munich Re: (1988), Financial Times (1992), Sigma Re: (1988-93), Pool (1991) BIIC and CEA Working Papers.

Regulation was tight in all four, state-controlled life insurance regulatory environments and is typical of a nationalised ethos. Yet in each Member State

changes were underway to allow greater freedom and enable competitive markets in line with the single market environment. Of the four state-controlled Member States, France had the most lax regulation in respect of life insurance. Each of the state-controlled structures had a different nationalised tradition and on the regulation matrix, they range between eight and eleven (see Life Insurance Regulation Matrix One, Fig 5.1 above). However, each Member State within this category was changing its legislation which would allow greater freedom in line with the impending SEM.

Regulatory Environment Survey and Analysis

To supplement the categorisation and provide further coding of the EU regulatory environments, a survey (survey A, Appendix A) was conducted to investigate the perceptions of life insurance companies throughout the EU. The main purpose of the questionnaire was to gain an understanding of how the Member State industries viewed their own regulatory environments and what they considered would be most advantageous for them at the EU level. The survey was sent out between Nov 1993 and Jan 1994 and was made up of 300 questionnaires (the sample was constructed on the availability of addresses) and a total of 121 completed questionnaires were received, broken down by Member State as follows;

UK = 36

Germany = 25

Netherlands = 15

Italy = 12

France = 17

Belgium, Spain & Eire (Other) = 16

Total = 121

No responses were received from Greece, Denmark, Portugal or Luxembourg. In the first three cases, this was due to translation problems and in all four Member States, there was a limited number of addresses for life insurance companies.

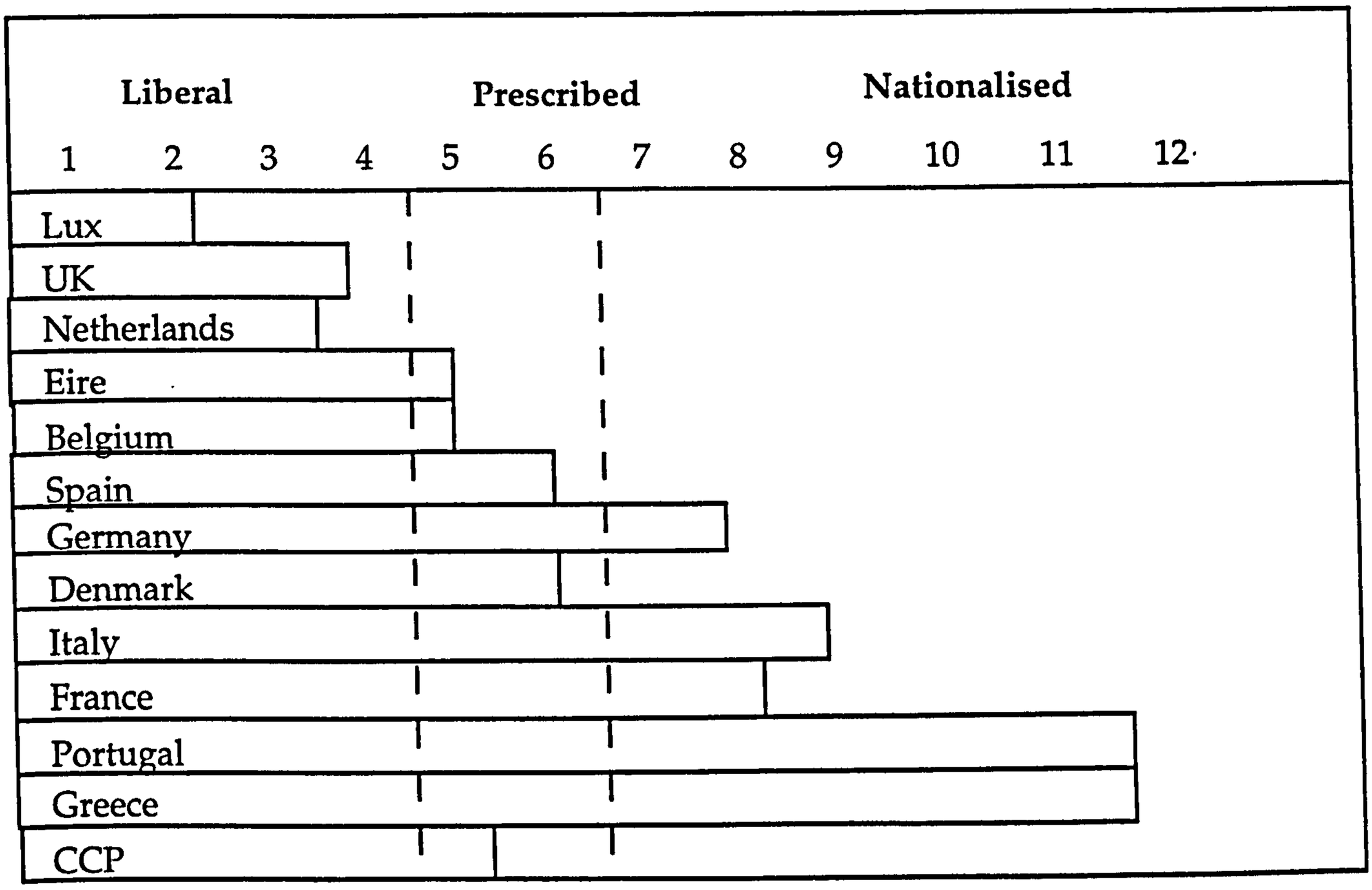
To provide a more objective analysis of the data, the results of the survey were added to the coding and comparative analysis undertaken above. This enabled a *postpositivist* analysis in that there is the recognition of an abstract reality juxtaposed with the inability of the human intellect to perceive it perfectly. Consequently, the thesis recognises that a perfectly objective comprehension of reality is always undermined by the subjectivity of the researcher and the researched. The comparative analysis indicated both the subjectivity of the author with the objectivity of the data itself, i.e. the legislation and subsequent regulatory environments. The survey results illustrate the subjectivity of the questions with the pursued objectivity of the respondents. These two sources compiled together attempt as objective understanding as possible, of the Member States' regulatory regimes and what they wished of the embryonic SEM in life insurance.

Table 5.2 **Perceived Regulatory Environment**

	Liberal %	Prescribed %	State Controlled %	Mean (SD)	Categorisation in Fig. 5.1
UK	66.7	33.3	0.0	4 (1.3)	Liberal
Germany	4.0	52.0	44.0	8 (1.9)	Prescribed
Italy	0.0	66.7	33.3	8 (1.0)	S/Controlled
Neth	93.3	6.7	0.0	3 (1.0)	Liberal
France	12.6	18.8	67.8	8 (2.3)	S/Controlled
Other	31.3	62.6	6.3	5 (1.6)	Lib/Prescribed
All	38.1	40.5	21.5	6 (2.4)	N/A

Fig 5.2.

Life Insurance Regulation Matrix Two



CCP = Compromised Convergence Point

Matrix compiled from an analysis of Munich Re: (1988), Financial Times (1992), Sigma Re: (1988-93), Pool (1991), BIIC & CEA Working Papers and survey of EU life insurance industry.

The respondents were asked five questions:

Question One asked how liberal or state-controlled they believed their own national life insurance regulatory system to be. As with the comparative analysis, the responses were categorised into liberal, prescribed and nationalised markets, for each of the eight responding Member States. The results of question one are summarised in Table 5.2.

The responses summarised in Table 5.2 (Perceived Regulatory Environment p 155) were subsequently used to amend the regulation matrix (Life Insurance Regulation Matrix One, Fig 5.1 p 157). The means of the responses illustrated in Table 5.2 were averaged with the assessment indicated in Fig 5.1. This gave equal weight to both the initial coding and categorisation of the regulatory environments and the further open coding regarding the perceptions of the life insurance industry. Indeed, the further coding procedure led to only marginal changes to the categorisation of the markets, indicating a degree of agreement between the two sources of data (see Life Insurance Regulation Matrix Two Fig 5.2 p 160).

Question Two asked the companies where they would position the SEM at that moment in time in respect of its regulatory environment. Again, this was on a scale of 1-12 and categorised the market types as liberal, prescribed and nationalised: the responses are summarised in Table 5.3. In general, there was agreement that the SEM as it stood was located between 7.0 and 5.0 with the mean of the responses of all Member States equal to 6.0, and a standard deviation of 1.5.

Table 5.3 Perceived EU Regulatory Environment

	Liberal %	Prescribed %	State Controlled %	Mean (SD)	Categorisation in Fig. 5.1
UK	13.9	69.5	16.7	6 (1.3)	Liberal
Germany	36.0	64.0	0	5 (1.5)	Prescribed
Italy	26.7	73.3	0	5 (1.6)	S/Controlled
Neth	35.7	64.3	0	5 (1.7)	Liberal
France	12.6	62.6	25.0	7 (1.3)	S/Controlled
Other	25.0	68.8	6.3	6 (1.9)	Lib/Prescribed
All	28.3	61.7	10.0	6 (1.5)	N/A

Question Three asked the respondents to indicate which type of regulatory environment would give their company its greatest advantage. The results are summarised in Table 5.4.

Generally, the Member States pursue market environments that are less regulated than or similar to their own. However, there are differences between the amount of liberality that each state considers should be allowed. This suggests that a compromise needs to be reached between the prescribed and liberal markets (such a compromise is shown in the Life Insurance Regulation Matrix, Two Fig 5.2, p 160).

Table 5.4 Perceived Most Advantageous EU Regulatory Environment

	Liberal %	Prescribed %	State Controlled %	Mean (SD)	Categorisation in Fig. 5.1
UK	72.2	27.8	0	3 (1.6)	Liberal
Germany	32.0	68.0	0	6 (1.3)	Prescribed
Italy	66.7	33.4	0	4 (1.9)	S/Controlled
Neth	92.9	7.1	0	3 (0.5)	Liberal
France	29.4	70.6	0	6 (1.4)	S/Controlled
Other	50.0	50.0	0	5 (1.2)	Lib/Prescribed
All	58.3	41.7	0	4 (1.5)	N/A

Question four asked what type of regulatory structure would allow the greatest consumer protection. Question five asked which would allow the greatest consumer choice. Each of these enabled an understanding of what the respondents considered a regulatory environment should entail and gave insight into their perceptions in respect of the first three questions. Responses are summarised in Tables 5.5 and 5.6.

Table 5.5 Best Perceived Environment for Consumer Protection.

	Liberal %	Prescribed %	State Controlled %	Mean (SD)	Categorisation in Fig. 5.1
UK	22.2	63.9	13.1	6 (2.3)	Liberal
Germany	20.0	56.0	24.0	7 (2.1)	Prescribed
Italy	50.0	50.0	0	5 (1.2)	S/Controlled
Neth	20.0	80.0	0	5 (0.9)	Liberal
France	11.8	52.9	35.3	7 (2.2)	S/Controlled
Other	25.0	62.5	12.5	6 (1.1)	Lib/Prescribed
All	30.8	53.3	15.8	6 (1.7)	N/A

Table 5.6 Best Perceived Environment for Consumer Choice

	Liberal %	Prescribed %	State Controlled %	Mean (SD)	Categorisation in Fig 5.1
UK	86.1	13.9	0	2 (1.5)	Liberal
Germany	96.0	4.0	0	2 (0.9)	Prescribed
Italy	83.3	16.7	0	4 (0.8)	S/Controlled
Neth	100.0	0	0	3 (1.0)	Liberal
France	70.6	17.7	11.8	4 (2.4)	S/Controlled
Other	88.1	12.5	0	3 (1.4)	Lib/Prescribed
All	87.6	10.5	1.7	3 (1.1)	N/A

These responses seem to suggest that the respondents were aware of what was meant by the term regulatory environment. Furthermore, there was a form of hegemony when it came to understanding the survey and the concept of a regulatory environment. However, this is more explicit in terms of the understanding of consumer choice. Indeed, in the construction of the Third Life Assurance Directive, it was around these very issues (the extent of interference regarding choice and protection) that the debates revolved. This is further illustrated in the next chapter.

Additionally, a series of cross-tabulations were undertaken and a verification of the independence of question one to the other four questions was performed. Two verification methods were utilised. Initially, verification was concerned with whether the respondents' perceptions of their current regulatory systems (question one) was independent of their perceptions of:

(a) the then present perceived EU regulatory system (question two).
(b) the preferred regulatory system (question three).
(c) the best regulation to ensure consumer protection (question four).
(d) the best regulation to ensure consumer choice (question five).

Firstly, the responses to question one were cross-tabulated sequentially with the responses to questions 2-5. Secondly, in each case, a chi-squared test of independence was undertaken. The results are illustrated in Tables 5.7-5.10

Table 5.7
Q1 - Q2

Perceived Existing SEM Regulatory Environment

Perceived current regulatory environment	Liberal	Prescribed	Totals
Liberal	14	32	46
Prescribed	9	40	49
State Controlled	6	20	26
Totals	29	92	121

$$\chi^2 = 2.07 \; (\chi^2_{crit} = 5.99)$$

In this case, the hypothesis of independence at 5% level of significance cannot be rejected.

In general terms, prior to the Third Life Assurance Directive, the Member States did not consider that their regulatory environments were similar to the SEM in general.

Table 5.8 suggests that Member States, when pursuing the SEM, would generally look for a regulatory environment either similar to or a little more liberal than their own. This is supported by the dependency ratio which suggests that the responses to question one are not independent of the responses to question three. That is, if respondents thought they had a liberal environment, they would like the SEM, to be more liberal or created in their own image. This is also indicative of the prescribed regulatory environments. However, the state- controlled Member States are generally looking for prescribed regulatory environments and some for the more liberal. Indeed, there is a shift toward more liberal/prescribed regulatory environments, with none wishing to remain state-controlled. Consequently, in the creation of the SEM, the sticking point would be found between the degree of prescription and liberality within the new environment.

Table 5.8
Q1 - Q3

Preferred SEM regulatory environment for company

Perceived current regulatory environment	**Liberal**	**Prescribed**	**Totals**
Liberal	40	6	46
Prescribed	21	28	49
State Controlled	8	18	26
Totals	69	54	121

$$\chi^2 = 28.14 \; (\chi^2_{crit} = 5.991)$$

In this case the hypothesis of independence can be rejected at 5% (and 1%) levels.

Tables 5.9 and 5.10 illustrate that there is a general perception that prescribed environments are better for consumer protection with 64% of those in liberal environments agreeing with this. Additionally, there is nearly unanimous agreement that liberal environments allow for the greatest consumer choice. In both instances, the thesis was able to reject independence at the 5% level between the responses to questions one and questions four and five.

Table 5.9
Q1 - Q4

Regulatory environment best for consumer protection

Perceived current regulatory environment	Liberal	Prescribed/Nat	Totals
Liberal	15	27	42
Prescribed	6	43	49
State Controlled	7	23	30
Totals	28	93	121

$$\chi^2 = 6.86 \; (\chi^2_{crit} = 5.99)$$

In this case the hypothesis of independence can just be rejected at the 5% level of significance (but not at the 1% level).

A final area of verification was concerned with investigating whether the respondents' preferred SEM regulatory system (question three) was independent of questions four and five. In both of these tests, independence is rejected. Thus there appears to be a link between the type of market preferred at the European level and what the industry considers as best for the consumer in terms of protection and choice.

Table 5.10
Q1 - Q5

Regulatory environment best for consumer choice.

Perceived current regulatory environment	Liberal	Prescribed	Totals
Liberal	45	1	46
Prescribed	40	9	49
State Controlled	21	5	26
Totals	106	15	121

$$\chi^2 = 8.01 \; (\chi^2_{crit} = 5.99)$$

In this case we can reject the hypothesis of independence at the 5% level of significance (but not at 1% level).

Table 5.11

Q3 - Q4

Regulatory environment best for consumer protection

Preferred SEM regulatory environment for our company	Liberal	Prescribed	Totals
Liberal	25	3	28
Prescribed	33	41	74
State Controlled	8	11	19
Totals	66	92	121

$$\chi^2 = 16.6 \; (\chi^2_{crit} = 5.99)$$

The hypothesis of independence can be rejected at the 5% and 1% levels.

Table 5.12

Q3 - Q5

	Regulatory environment best for consumer choice		
Preferred SEM regulatory environment for our company	**Liberal**	**Prescribed**	**Totals**
Liberal	68	1	69
Prescribed	38	14	52
Totals	106	15	121

$$\chi^2 = 17.7 \; (\chi^2_{crit} = 3.84)$$

Again the hypothesis of independence can be rejected at 5% (and 1%) levels

Conclusion

Through the comparative analysis of Member State legislation, open coding and categorising, the information accrued from the survey and study of the Member States legislation, we have constructed a regulation matrix. This thesis proposes that through the political impetus of the SEA, legislation is being reformed to meet the needs of what is becoming the normative perception of the evolving SEM. However, it also proposes that the normative concept of the SEM is tempered by the ideas that the industries have of their own trading structures and that these will differ from one Member State to the next, because each is used to trading in a distinct regulatory environment. This is explicit in the Third Life Assurance Directive with reference to both the process of formulation and the end result. As a nationalised market environment is out of the question in respect of the basic tenets of the Treaties and present competition policy, the compromise is taking place between the prescribed and liberal regulatory environments and

it is here that agreement was being reached and a new environment formed, through the concepts of harmonisation and mutual recognition.

The nationalised and greater prescribed environments indicate the convergence process with the greatest clarity as these markets are being forced into bringing their supervision into line with the less regulated markets. However, the more liberal regulatory environments also need to change legislation to bring them into line with European directives. The less prescribed and less liberal markets have the fewest changes to make and this is apparent in their adroitness at bringing in the directives. This is particularly so of Belgium and Eire and to a lesser extent Spain, Denmark, the UK and the Netherlands.

The responses to the survey from the UK and Dutch life insurance industries do reveal a preference for a more liberal market than is perceived to be the case in much of Europe, and one very similar to what is generally understood to be their home market conditions; in short the liberal life industries want the new market to be as similar to their own as possible to allow greater certainty and profitability. The prescribed markets want greater freedom but not enough to put them at a disadvantage in relation to the liberal markets. Finally, the state-controlled industries want less regulation on their trading structure. However, the Italians seem to want to pursue a liberal environment, whereas the French would remain with one that was highly prescribed.

The matrices and tables attempt to identify a compromise point between the Member States. They also allow a more elucidating comparison between the Member State legislative regimes in relation to a specific market. Indeed, it contends that compromise between the Member States allows a directive to be

established between 4.5 and 6.5 and that through mutual recognition these points are integrated at the compromise convergence point (5-6 on the matrix) (see Life Insurance Regulation Matrix, Two Fig 5.2 p 170). However, in the initial negotiations, Member States and national industries are generally looking for legislation as similar to their own as possible, i.e. the UK pursuing a three and Germany a six. Through compromise and a recognition of what the Commission and Europe perceive as necessary, the parameters of a directive are established (this will be discussed further in the following two chapters). This adds an impetus to integration through the recognition of a European market and calls for harmonisation in further areas. This illustrates spillover to the extent that further legislation will be necessary in life insurance and other financial sectors i.e. banking and capital markets. It also illustrates supranationality because the needs of the Commission and Treaties are built into the legislation. No one Member State gets all of its own way: the legislation is both a compromise and one which reflects a European perspective.

In general, the frequency tables and cross-tabulations support the view that each Member State is pursuing its own *self-interest* in the creation of the new market. The thesis now asks where and how does compromise takes place? To answer this question, we examine the creation of the Third Life Assurance Directive in Chapter Six, and through a number of interviews undertaken at the European decision-making level in chapter Seven. The thesis considers that through identifying interaction between interest groups, supranationality and spillover, neo-functional and intergovernmental processes may be defined, explored and understood.

Chapter Six

Institutional Roles in EU Decision-Making: A Case of the Life Insurance Industry

> *Behaviour is ultimately a social matter . . . and thinking in terms of what 'we' should do, or what should be our strategy, may reflect a sense of identity involving recognition of other people's goals and the mutual interdependencies involved (Sen, 1992; p 85).*

Introduction

"Wyn Grant has noted that the relationship between pressure groups and the European Community has, so far, been a relatively neglected subject. In Britain, there are very few general studies of groups trying to influence EC decision-making" (Mazey and Richardson, 1993; p 93). "Direct lobbying of EC institutions constitutes an important part of the decision-making process within the Community and has the effect of increasing EC autonomy over the interests of Member States. There has been a rapid expansion of such activities over the last few years. However, although this phenomenon has attracted a lot of attention, there is surprisingly little systematic research on the topic" (Andersen and Elliassen, 1991; p 173). In addition to a number of recent studies this thesis is attempting to address this neglect (see Greenwood *et al*, 1992; Greenwood, 1995; 1997; Maloney, 1993; McLaughlin *et al*, 1993; McLaughlin and Greenwood, 1995; McLaughlin, 1995).

This chapter provides an overview of the workings of the EU decision-making processes regarding the negotiations and formulation of the Third Life Assurance Directive. In this context, it identifies embryonic supranationalism in the EU institutions and the extensive use of interest groups in legislation formulation. Interest groups will be defined as non-governmental organisations that attempt to have an influence on public-policy. They are entities that provide an institutional linkage between sectors and government. More precisely they are " . . . those types of organisations whose political task it is to reflect the interests of the economic or occupational sections they represent" (Lieber, 1974; p 29). Indeed, interest groups are described as,

> . . . those organisations which are occupied . . . in trying to influence the policy of public bodies in their own chosen direction. . . . European interest groups . . . are centrally organised associations of interest groups . . . each of which represents either a number of similar groupings or both national groupings and European industry committee groupings (Kirchner, 1980; p 96).

Interest groups apply pressure. Consequently, the terms pressure group and interest group will be used inter-changeably. Interest groups can either be of a sectional or of a promotional nature. We concentrate here on the sectional interest group category which usually represents the interests of professions, producer groups, occupations or trade unions. In particular, we concentrate on the sectional interests of the life insurance industry.

In the 1990s, following the SEA and the Maastricht Treaty, a number of research projects on European business interest groups were undertaken.

Mazey and Richardson (1993) conducted a number of empirical studies but according to Grant (1995) overall the research picture was still opaque.

> There is little consensus about the importance of different types of interest groups, about the influence they can exert on the politics and policies of the EC and the effect their activities have on the development of the integration process (Kohler-Koch, 1994; p 166, cited in Grant, 1995; p 99).

However, the importance of interest groups in the European decision-making process had been recognised, hence the time and effort that is now being spent on them.

> Since the early 1980s . . . growing numbers of organised interests . . . have come to recognise the increasing importance of European Community legislation . . . It is no longer possible to understand the policy process . . . without taking account of the shift in power to Brussels (Mazey and Richardson, 1993; p 191).

Indeed, the SEA created an impetus for the use of interest groups. With Qualified Majority Voting (QMV) and the SEM programme, lobbying in Brussels became imperative. "However, as several groups discovered to their cost, lobbying in the European Community is far from a simple matter" (ibid). In Europe, the process of lobbying is far from a 'cloak and dagger' scenario, it is quite the opposite. In Brussels, lobbying is open, uncertain and unpredictable. "Thus, in order to be effective Euro-lobbyists, groups must be able to co-ordinate their national and EC level strategies, construct alliances with their European counterparts, and monitor changing national and EC policy

agendas" (ibid, pp 191-192). Indeed, the European institutions (especially the Commission and the Parliament) have been

> . . . approached directly . . . (and) the two EC institutions have developed a comprehensive network of contacts that cut across, and are independent of, member countries. Increasingly it is necessary for lobbying to be based on broad alliances representing a more European perspective. We might think of this process as Europeanisation (Andersen and Eliassen, 1991; p 174 author's brackets).

Some commentators consider that sovereignty has increasingly been ceded to the European institutions and that decision-making in the European Union is a balance between intergovernmentalism and the supranational institutions. In the majority of economic areas, it is generally impossible for one Member State to pursue total self-interest because self-interest has become bonded to the other Member States; ". . . national self-interest has partly become a collective European interest . . . forty years of working together has resulted in collective outputs being produced and recognised by the parties involved" (Greenwood, 1995; p 2). The European Commission and Parliament consider that speaking to European organisations allows an understanding of European-wide interests. Indeed, to ensure effective lobbying it is necessary to build coalitions.

Both the European Commission and the European Parliament frequently stress that they want to speak to European organisations. Where possible, therefore, you should seek to build coalitions, and the more representative they are in terms of the sector(s) a proposal will affect, the better. Of course, your

> interests might be at odds with other companies . . . operating in the same sector as you . . . (and) if they have a good argument and their interests are at stake, companies may be forced simply to lobby on their own behalf (Club de Bruxelles, 1994; p 96 author's brackets).

Camerra-Rowe (1996) points out that different sectors can undertake different strategies when it comes to lobbying European institutions. She considers that on the one hand, the insurance and pharmaceutical sectors have well run interest group representation at the EU level. While on the other, the likes of the bio-technological and automobile sectors companies represent themselves directly at the EU level. Direct lobbying more accurately indicates a company's choices. However, this is expensive and there is no certainty that the Commission or European Parliament will listen to an individual company if its proposals are not similar to the EU's or the sectors objectives. But this does illustrate that on certain matters the concerns of individual companies will be taken into consideration. "While the Commission prefers dealing with associations, its officials have been relatively open to lobbying by individual large firms. Thus, firms often have an incentive to lobby directly. . . . However, it is rare for a firm, even a large one, to rely on one channel of representation" (ibid, p 6). This provides the basis for a number of difficulties. Companies that lobby directly:

(a) undermine the role of interest groups because the message they carry may not represent the whole sector;

(b) have limited incentives to compromise their positions in the collective because they are able to lobby themselves;

(c) force the association to reach consensus; this may lead to the acceptance of the lowest common denominator and undermine the effectiveness of the interest group.

Small and medium-size enterprises or companies that are incapable of lobbying the EU directly intensify the role of the interest group. Members are forced to accept sector compromises and they cannot use the interest group to pursue private advantage. European interest groups ". . . therefore have greater flexibility in the types of positions they take . . . it means that the association has greater political weight because it can claim to speak on behalf of all members" (Camerra-Rowe, 1996; pp 6-8). Of course, the other extreme is where the interest group is so diverse in its membership that agreement can never be reached. As in most things, balance is of the essence.

The European insurance sector is mainly made up of small and medium-size enterprises and with the exception of Allianz, lack the political clout and resources to undertake direct action in Brussels. As a result, both national and European interest groups have a greater influence on the Commission and their membership. Companies need to accept the interest group's ". . . policy position even if it does not take account of their particular interests because they cannot effectively represent their own views. As a result, and paradoxically, the more fragmented insurance sector was better able to undertake collective activity in pursuing Community policy" (ibid, p 21).[1] In

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[1] It is considered that the less concentrated a sector is the less difficulty it has in overcoming the problems of collective action. For instance, the automobile, biotechnological and consumer electronics sectors interest groups have been relatively weak, whereas in the pharmaceutical and insurance sectors interest groups have greater influence. (for further see Camerra-Rowe, 1996; McLauchlin and Jordan, 1993; Greenwood and Ronit, 1992; and Cawson 1992). There is an interesting dilemma with regard to these different ways of lobbying the EU. If one uses interest groups successfully then is the sector adhering to neo-functional processes? Alternatively, if a company lobbies the EU directly is it adhering to neo-corporatist processes? This thesis considers that both understandings are very similar as each has lobbied a supranational institution and each has taken part in a marginal shift in sovereignty. It may be argued that it is this shift that is important, not how it was achieved. The EU is an evolutionary process as are its institutions and this is illustrated by the uncertainty of the final (if such occurs) formalisation of relations between interest groups and the EU. Camerra-Rowe (1996) considers that it is unlikely that interest groups will be the prime movers in interest representation in the EU. That the ". . . initiatives the Commission and other EU institutions undertake to regulate interest groups will be critical in determining the future form and shape that business representation takes. . . . In short, effective collective action may originate not from the desire of firms in these sectors to

this chapter, we examine the initial discussions regarding the legislation and regulatory regimes that should be pursued to create the market most amenable to all Member State life insurance industries. Fundamentally, we consider how effective interest groups were in the creation of legislation and the consequent regulatory environments.

The Comité Européen des Assurances (CEA)

Insurance interest representation at the EU level is primarily undertaken by the Comité Europeén des Assurances (CEA) which has operated since 1953. Indeed, it is an organisation that existed before the creation of the EEC and this is reflected in its membership (this is not made up solely of Member States). "Nevertheless the single most important function of the organisation is to work through its 'Common Market Committee' which is officially recognised by the EU and through which all insurance directives pass" (Vipond, 1995; p 105). This is reflected by the Commission which considers itself as an organisation that is always open to external input and Commissioners welcome this input. Indeed, the Commission has ". . . a reputation for being accessible to interest groups . . . (because) it is in the Commission's own interest to do so since interest groups can provide the services with technical information and constructive advice" (OJ/C 63/02 author's brackets).

The DGs see the CEA as the main representative of the insurance industry. Such was reiterated by Leon Brittan in 1989,

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speak with a common voice on common interests, but from the desire of EU officials to create common collective interests from a multitude of private ones" (p 23). Either way there is an emphasis on creating certainty and even though there is a detraction from pure neo-functionalism, it is a supranational entity creating the rules and a shift in allegiance has taken place (Haas, 1958).

the CEA has proved its worth . . . as a standard bearer for the insurance industry at the European level. I know that DG XV has come to rely greatly on the CEA and its officials . . . as an organisation which is fully representative of the insurance industry, which puts your views and concerns to us frankly and powerfully and defends them tenaciously (Sir Leon Brittan, speech given to the CEA November 1989; cited in Camerra-Rowe, 1996; p 18).

These sentiments were supported in a number of interviews undertaken by the author (see Chapter Seven). Indeed, they reflected the results of a set of interviews undertaken by Camerra-Rowe in which a Commission official said that ". . . they (the Commission) have almost institutionalised corporatist - like relations with the CEA" (ibid, p 18 author's brackets) and those provided by Mazey and Richardson (1996).

A Single Market in Life Insurance: The Initial Discussions

The discussions about a single market in life insurance began in earnest between 1987 and 1988, and it is at this point, that interaction between the different elements of the decision-making apparatus becomes more recognisable. In this study each of the decision-making areas are investigated and the means by which they interact with the others is overviewed. The thesis concentrates on the following aspects of the decision-making process: national interest groups; European interest groups; national supervisory authorities; the Commission; European Parliament; and the Council of Ministers. Because of the impetus the SEA and the White Paper (1985, 1986) gave to the construction of the internal market, there was a greater emphasis on creating a single market in financial services. This was accompanied by a

streamlined decision-making process which necessitated compromise and interaction between the Member States on most issues. Hence, there was a shift towards a more concerted effort in the creation of an SEM in life insurance.

The starting point was the realisation that regulation differences were the main factors undermining the creation of a SEM in insurance. With regard to this, the Commission considered that its main objective was to create co-ordinated insurance supervision throughout the EU. Little work needed to be done on reinsurance because Member State reinsurance markets were least different in legislative terms. However, at the other end of the scale:

> . . . divisions appeared most marked in life insurance, where national ideas on consumer protection, the promotion of the economy, currency protection, social objectives and taxation were combined with different attitudes to composite insurers and even divergent conceptions on the scope of life insurance itself . . . for this reason . . . life insurance has been left until last at each subsequent stage (Pool, 1992; p 179).

Freedom to provide services throughout the EC is intended to make it possible to exploit the local advantages of production *vis-a-vis* the customers of other sectors. In both cases the trade barriers contained in the legal framework conditions should be reduced as far as possible by harmonising laws. . . . In this respect the efforts of the EC Commission to achieve harmonisation have . . . been duly recognised. Yet - however much one approves of the objectives of the EEC Treaty - harmonisation has its limits, particularly because of differences in legal culture,

> sense of justice and the extent to which Member States are prepared to comply with the law (Jur *et al*, 1989; p 16).

Dickinson (1990) contended that a common market in life insurance means

> . . . both the freedom of insurance companies to supply and the freedom of consumers to buy in any country within the Community . . . In addition, an insurance company should be free to supply any life insurance and private pension product that it considers has a market demand. This should be combined with the freedom to price and market that product, using a distribution channel that it considers appropriate (Dickinson, 1990; p 97).

The products a life insurance company may supply are defined by the local insurance company acts. "Legislative environments vary significantly across the Community . . . this variation is due to differing local market and regulatory traditions (ibid, p 98). Dickinson was indicating the need for a liberal life insurance services directive.

The Treaties illustrate the political dimension of the process. It is the responsibility of the Commission to pursue the tenets of the Treaties and in doing so bring to the process legislative ideas of their own. Effectively, there is an interaction between the industry (in European and national terms) and the Commission. However, there are differences both between the Commission and the industry and among the different Member State industries. This is because of the national perspectives of what life insurance is and how the industry should be governed.

Pool (1992) considered that ". . . insurers are certainly much better organised as a pressure group than the other players in the insurance markets. Even they, however, have not always found it easy to arrive at a common perception of what a common market should mean for them" (p 11). For many years the CEA has acted on behalf of its membership with regard to European issues. There are also Member State national interest groups that are affiliated to the CEA. The main objectives of European interest groups are two-fold. Firstly, they should ". . . promote the exchange of information and try to find common denominators (consolidate strength)" (Kirchner, 1980; p 109). Secondly, they should ". . . co-ordinate and exert pressure for adopted policies through the European organisations and the national affiliations on both the EC and the national government" (ibid). Interviews, undertaken by the author indicated that it was very rare for European interest groups and national governments to interact; this is done more usually by their affiliates (the national interest groups).

European interest groups attempt to keep their membership informed about developments in the sector and on EU activities. They achieve this through holding seminars and conferences on important issues. Essentially, they try to ". . . instil a spirit of co-operation and cohesion into their affiliates" (ibid, p 110). In this context, they are performing the role assigned to them by neo-functionalism: a means of integrating ideas, creating compromise and interacting with a supranational body. They act as a catalyst in the transferral of allegiances by national actors away from the national to the European decision-making arena. As discussed above in Chapter Four (see Haas, 1958), the supranational entity in this context is a coalition of the European Commission, the Council of Ministers and European Parliament. This is the

shift toward a supranational decision-making entity and it is in this context that we examine the formulation of the Third Life Assurance Directive and the actions of those involved in its creation.

In 1995, the Director-General of the ABI (Mark Boleat) asked whether or not the Single European Insurance Market had arrived and if trade associations and legislators could ". . . sit back and let insurance companies get on with putting the new freedoms to practical use" (Boleat, 1995; p 45). His answer to this was "no": the industry needed to remain diligent because insurance is a complex financial service and has the potential to impact on many parts of our existence. To this extent, many proposed directives would have implications for the industry which should consequently ". . . influence the debate . . . be aware of new proposals and . . . submit their views at an early stage so that the implications can be properly considered and any necessary changes made before the proposals become set in stone" (ibid).

"Commerce, which has enriched English citizens, has helped to make them free, and this freedom in its turn has extended Commerce, and that has made the greatness of the nation" (Voltaire, 1980; p 51). Frangoulis (1988) points out that such a heritage is still apparent and for the

> . . . British insurer freedom is the 'zero option', meaning minimum interference with market forces in a capitalist society and the right of free choice for the buyer. Without free choice, commerce cannot be extended, whether within or outside the Community (p 1).

He considers that the most difficult element in creating a single market in life insurance ". . . is the existing differences in supervisory regimes" (p 2).

However, it was recognised by the CEA that differences ". . . in the supervisory practices of Member States could lead to distortion of competition between insurance undertakings. Harmonisation of supervisory methods therefore appears necessary" (CEA Working Paper, 1990; p 4).

In 1988, Frangoulis predicted that over the first four to five years there would be little change. Initially, ". . . buyers, brokers, carriers of insurance, will have some difficulty in coming to terms with the rules of the game" (Frangoulis, 1988, p 6). This is because ". . . the structure of future programmes of insurance will call for a totally new approach in terms of comparability of cost, contract terms, quality of security etc. These things take time" (ibid, p 7). This was reinforced by O'Leary who suggested that ". . . we start with a rather more limited form of freedom and gradually progress towards the ideal of complete freedom (O'Leary, 1988; p 2). Effectively, there will be difficulties for insurers when they attempt to formulate new strategies as new regulations are bound to affect operations. It was felt that this would also be the case for UK insurers and that they would need to revisit their tactical and strategical operations in a post-1992 environment.

Initially, it was thought necessary to revisit the accepted division between home and overseas markets and the view that companies are not interested in offering cross-border services because they are designed to operate through establishments: this leaves a large hole in the corporate structure. "The market place is not there to accommodate insurers, it is the insurers who should fit the market" (ibid). Additionally, new skills would be necessary to enable market penetration i.e. the EU markets would need to be understood.

O'Leary[2] (1988) drew attention to the feelings of many UK insurers and their inability to take the SEM as seriously as their continental counterparts. His hope was that such would not continue to be the case as change is continual in the creation of the SEM and it was crucial that the UK had an input into the formulation of the market. He recognised that in Member States the two areas legislation is concerned with are consumer protection and limitation of policy-holder risk. "However, the way in which this is done differs from country to country" (ibid, p 1). For instance, in the UK, companies were allowed a large amount of freedom in relation to some of their EU counterparts. In other Member States, this was not the position. Instead, the regulatory structure was much tighter. However, most consider that the UK's system of consumer protection is insufficient.

> Now I hold exactly the opposite view, I think that our system is better for the consumer and that the result of the continental system is that the company is protected from failure . . . and that although the policy-holder is protected from loss this is at a very high price. . . . Our policy-holders have higher returns . . . a wider choice . . . (and) a high level of guarantee that their return will be adequate even if the company gets into trouble (ibid, p 2 author's brackets).

On the other hand, the prevalent system in the EU allows high security for both the company and the policy-holder but at the cost of restricted policy choice and indifferent investment returns.

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2 O'Leary was the representative of the British Insurers International Committee (BIIC). The author has interviewed him and the results are transcribed below in Chapter 7.

O'Leary (ibid) considered that there were a number of problems between the UK and more prescribed Member States with regard to legislation covering the Third Life Assurance Directive. These included problems with uniform premium rates: this is where the supervisory authority indicates the bases to be used in premium calculations so creating nearly identical premium rates across the product. The UK does not have these restrictions. Secondly, he pointed out that in most Member States the authorities also control policy conditions and this has undermined the adaptability and range of products. Thirdly, in a number of Member States, the authorities indicate the extent of the companies' investment policies. In each of these areas, the UK has less regulation and in most cases no such restriction. Consequently, for a free market to be established, a harmonisation process has to be undertaken. Other difficulties that were being dealt with at the time (1988) included a uniform approach to reserving and the transmission of premiums from one Member State to another. Additionally, insurance contracts caused a problem, as they did throughout the early 1990s.

> Article 25 contains a marketing rule for insurance products . . . to the single case of contracts in conflict with legal provisions protecting the general good in the Member State in which the risk is situated. The concept of general good . . . must be understood in the light (that) . . . derogation's to freedom laid down by the EEC Treaty are only allowed where there exists in the area considered, mandatory reasons linked to the general good (consumer protection rule) providing that this interest is not already safeguarded by rules to which the undertaking is subject in the Member State in which it has its head office . . . and providing that the same result cannot be obtained by less stringent rules (CEA Working Paper, 1990; p 2. For further on

this see ECJ's decision Case 205/84 *Commission v Germany (Re Insurance Services)* [1986] ECR 3755 in particular recitals nos 27-29 author's brackets).

Indeed, the

> . . . general good is a judge-made concept, developed in the case law of the EC Court of Justice. It allows Member States, in the absence of harmonisation of the rules applicable to services or of a system of equivalence, to maintain certain national measures, although such measures may constitute a barrier to the free movement of goods, services and establishment, and workers (Van Schoubroeck, 1994; p 149).

In the field of insurance services, the concept of the general good has come to play an important role. This is so, ". . .first of all, because Community insurance directives regulate only partially cross-border insurance activities, and leave room for Member State regulation. Secondly, these insurance directives refer explicitly to the general good in relation to the regulation of insurance activities in general and insurance products in particular" (ibid, p 152).

Basically, it would be necessary to monitor the concept of general good very closely if it was not to become an NTB.

Another area felt to undermine the idea of the creation of an SEM in life insurance was taxation;

(a) taxation on premiums.

(b) taxation of benefits.

(c) taxation on the insurance companies.

Theoretically, these problems could be overcome by taxing the policy-holder in terms of residence and taxing the company with regard to where the head office is situated. However, this was largely academic because tax legislation was excluded from the Third Life Assurance Directive because its inclusion would have necessitated unanimity instead of a qualified majority.

In 1988, it was unclear what would be included in the Third Life Assurance Directive. What was necessary was dialogue with the insurance industry. When Pool spoke at a meeting of the Double Century Club with regard to the directive he contended that:

> . . . he did not know what was going to be in the directive and that he was open-minded and listening to the views of the market . . . he felt that research is required to identify the legal framework or frameworks existing in each Member State . . . and he has asked the CEA to study the position (O'Leary, 1988; pp 4-5).

However, at a later date Pool pointed out some fundamental problems in the pursuit of a SEM in life insurance.

One such pair of apparently incompatible goals is the desire for increased competition coupled with greater consumer protection. Of course, in many areas of commerce increased competition is itself the best consumer protection. This will be so where the buyer can easily compare products and prices and can judge for himself what he is getting for his money. This is not so

> easy in insurance, where the policy-holder pays money in advance in return for promises expressed in a contract (Pool, 1990; p 9).

For this reason, market forces are seldom perceived as the most satisfactory solution. The problem is that controls both reduce competition and create protectionism. "It is also true, however, that different perceptions of public interest and different degrees of State intervention produce a situation in which mutual recognition . . . is hard to attain" (ibid, p 10). Consequently, a degree of harmonisation was necessary to bring separate Member State industries into the same legislative realm. Pool, felt that there was a growing view in some Member States ". . . that some of the tight controls exercised in the past had been too restrictive of competition and of little practical use in protecting the public interest" (ibid). Such was indicated in Chapter Five above.

"In the UK there is considerable opposition to any illiberal restrictions. In the continental countries there is a great fear of the UK as competitors and a, genuine if misguided, belief that strict supervision is the only effective method of consumer protection" (ibid, p 6). Ultimately, it was considered that there was ". . . the need for a high degree of harmonisation"(ibid). The interests of the UK lay with a free liberal regime and the British Insurers International Committee (BIIC), the negotiating arm of the Association of British Insurers (ABI), with regard to Europe, pushed for this position to be adopted. Of course, other Member States also pursued their ideal solution.

The problem was to achieve a single market in life insurance through the harmonisation of legislation that determines their individual regulatory regimes.

In insurance the existing national markets differ significantly in the nature and amount of regulation. They also differ in the nature and variety of products that can be offered. The problem we confront is therefore how to reconcile the objective of liberalising the markets, and of offering the consumers as wide a range of choice as possible with that of satisfying the authorities in all Member States that there is adequate protection for the policy-holder and third parties (Fitchew, 1988; p 1).

The Deputy Chairperson of the then EEC standing committee of the Bureau International des Producteurs D'Assurances et des Reassurances (BIPAR) considered that the UK insurance industry did not seem to be taking the EU seriously. Gale (1988) emphasised the role of BIPAR in the creation of legislation and the extent to which this organisation interacts with the Commission. He indicated that the Treaties have supremacy over national law and that Member States cannot be part of the club and disobey the rules. "Suffice it to say that as a result of representations made by me and my BIPAR Common Market Committee, DG XV will be mounting a concerted exercise, initially of persuasion, to establish a more level legislative playing field" (ibid, p 7). Primacy of EU law, for Gale, should benefit the whole of the EU ". . . since it must result in the rapprochement of our diverse legal systems which will eliminate many doubts and disparities which currently bedevil us, particularly at the commercial level" (ibid). Indeed, Gale points out the supranational aspect of the EU in that it negotiates on behalf of the Union at the international level e.g. GATT, now the World Trade Organisation (WTO). Given the importance of the negotiations to the insurance industry, he has regular contact with those in the Commission that were responsible for negotiations. Ultimately, as Deputy Secretary of BIPAR, Gale looks to the

interests of his membership who through interest group membership ensured that their interests were on the table. "1992 equals opportunity . . . but only if you understand exactly what you are doing and are well aware of the details of the environment in which you will be operating" (ibid). In this context, each industry will be pursuing legislation as near to their own as is feasibly possible given the remit of the Treaty. Therefore, each Member State should be involved in the creation of each directive to ensure their advantage in the embryonic SEM.

This had become much clearer by 1990 and was illustrated by the extent to which interest groups were involved in the European decision-making process. It was accepted that the industry could learn from itself as the CEA, and other European insurance associations, were invited by the Commission to give their views. And where the European insurance industry as a whole was supportive of the opinions expressed by the Commission, one had a strong suspicion that they would shape the outcome.

The CEA, the Commission and the European Parliament

This section of the chapter will overview the interactions between the interest groups and the supranational institutions. This is further analysed in Chapter Seven where interviews with those involved in the actual process of creating the Third Life Assurance Directive are summarised and discussed.

"A major problem for groups is the unpredictability of the EC policy-agenda . . . Keeping track of EC policy initiatives is therefore a major undertaking for groups" (Mazey and Richardson, 1993; p 206). For instance, changes may be brought about because of European Summit decisions or because of different political agendas that certain Member States may have. Additionally, the

Commission's policy agenda is also unpredictable because of its make-up or its compartmentalisation into DGs. In the national sphere, interest groups face similar difficulties to those indicated above. However, the difference is of degree and the difficulties incorporated in dealing with fifteen Member States' inputs to the policy process and its openness and size (it is relatively small and lacks expertise and technical knowledge regarding all Member States). "It is therefore reliant upon external evidence from groups or experts . . . the desire on the part of Commission officials is to consult as wide a range of groups as possible, means that it is virtually impossible for any single interest or national association to secure exclusive access to the relevant officials" (ibid, p 209). Interest groups provide information for the Commission and give an overall picture in this instance (a compromised view) of the most amenable regulatory structure for European life insurance. Only European interest groups can do this as only they are able to have even a marginal understanding of what the majority wish to pursue.

Through its central position in the legislative process, the Commission is able to comment on ". . . the feasibility of new EU policies, a role that requires the (it) to solicit expertise . . . (from) state executives . . . sub-national authorities, and a large variety of interest groups (Hooghe and Marks, 1997; p 28 author's brackets). Furthermore, ". . . its position as interlocutor . . . gives it unparalleled access to information" (ibid). The Commission considers that it is always open to external input and that the process is invaluable in the creation and development of policies.

> The Commission has in particular a reputation for being accessible to interest groups and should of course retain this ease of access. Indeed, it is in the Commission's own interest to do so since interest groups can provide the services with technical

information and constructive advice. . . . The Single European Act along with the White Paper programme, prompted a sharp increase in lobbying at Commission level. At the same time there was a shift in the need for information from a general to a specific level. Evidence of this is that independent consultants began to obtain monitoring contracts from clients. Moreover, organisations sought to exert influence. . . . In addition some of these special interest groups serve as a channel to provide specific technical expertise to the Commission from a variety of sectors, such as the drafting of legislation (OJ 93/C 63/02).

Leon Brittan outlined the Commission's position at a CEA meeting in November 1989. He contended that there were two broad objectives: firstly, policy-holder protection in terms of the products offered and the financial position of the insurance undertaking; and secondly, ensuring the maximum flexibility of product in terms of nature, price and service. This should allow the policy-holder a wide choice of products at competitive prices. The problem was that most Member States (with a little fine-tuning) considered that this was exactly what their regulatory regime achieved. Obviously, this agreement hides underlying discord with regard to the means applied by the separate Member States. The problem reflected the historical and cultural differences within the Member states.

In general, there are two broad approaches; the liberal approach and the prescribed approach. The UK, Netherlands, Luxembourg and Eire illustrate gradients of the former and the other eight Member States have elements of the latter (with Italy, France, Greece and Portugal bordering on state-control). This situation was outlined in the previous chapter and indicated the difficulties apparent in negotiating a SEM in life insurance. These differences

of opinion can be identified in the overall stance of the CEA and become explicit in the negotiation processes. Obviously, the more different the viewpoints, the greater the difficulties for the Commission in its task of creating a system which is both agreeable to them and allows mutual recognition of the different systems. Consequently, agreement has to be reached at the industry level through the CEA and this agreement needs to be compromised with Commission objectives. Effectively, the European insurance industry along with the Commission and Parliament is looking for agreements and compromises that will carry a qualified majority at the Council level.

Initially, a broad framework was proposed by the Commission; then through the CEA, the European life insurance industry responded (this was the collective opinion of twelve Member State industries). The Commission concentrated on three areas: a single licence, home country control and the abolition of prior approval of premium rates and conditions. Additionally, technical reserves needed to be standardised. The CEA's response to this came under the auspices of five areas.

(a) Assets

(b) Reserves

(c) Premium rating

(d) Policy conditions

(e) Supervision

The non-life insurance directive enabled the framework for CEA discussions in the area of assets. Agreement was close to unanimous on a majority of important issues. There was unanimous agreement that a list of admissible assets should be defined by the Commission to supervise all Member States

and that these regulations should be pursued under home country control. Unanimity also prevailed in opposition to minimum limits on any specific category of investment. There was also general agreement in terms of the liberalisation of capital movements and allowing companies to benefit from the advantages of different financial markets. The two systems (current market value and investment at cost) that exist regarding asset valuation were covered by the accounts directive which considered that they should co-exist. Market value should show values at cost and *vice-versa*.

In terms of supervision, most Member States considered that an environment close to the prescriptive system of strict supervision would be best for the SEM. This would mean the Member State authorities stipulating a maximum technical interest rate which, following consultation with the EU, would be fixed by the supervisors. The more liberal states, including the UK, thought that this was too rigid and that a more flexible system, that gave more of a role to the company and actuarial judgement would allow local economies to be taken into consideration. This problem needed to be overcome if mutual recognition was to be realised, and all Member States were to feel that the supervisory provisions throughout the EU gave adequate security. This area proved a sticking point and much negotiation was necessary. On other matters concerning reserves, the Member States were unanimous, i.e. no need for a European mortality table, or local regulation of tables.

In the area of premium rates, once again, there were differences of opinion. In a number of Member States it is the practice to apply the same technical rate to both premiums and technical reserves with the supervisors placing ceilings on the rates that can be adopted. In the more liberal countries, such was not the case; companies were free to fix premium rates, subject to prudent

mathematical reserves, as there was no need for the rates used to calculate premiums and mathematical reserves to be the same.

The more prescribed Member States wanted the supervisory authorities to continue determining policy conditions and in some instances the host Member State should be allowed to intervene and have some say in policies sold in their own Member State. On the other hand, the UK wished to minimise legislative interference in the regulatory process; this implies minimum host country control and intervention. The CEA fully supported the abolition of prior approval for contractual conditions and rates as outlined by the third framework directive and its replacement by a system of notification (CEA, 1990). The CEA considered that under a system of single licence it becomes the responsibility of the authorities in the Member State where the head office is to supervise its activities.

The basic principle sought by the Commission was one where policies would be written under the legislation of the country of risk or normal country of residence. However, with regard to life insurance one is dealing with long-term contracts which may be taken out in different periods and will co-exist. Consequently, it was acknowledged that individuals should be able to take out contracts in line with their own Member State legislation even though they had changed their residence. It was agreed that profit sharing should be left to the company as this would enhance competition. However, the CEA did note that there was a minority that considered a more prescribed attitude in this context in that profit-sharing should be co-ordinated for long-term contracts.

With regard to supervision, the majority of Member States considered that the host Member State should have a part in the determination of contracts to

be sold in their territory. They thought that unless they could control contracts they would be unable to protect policy-holders. The UK, of course, did not share this viewpoint. However, the majority agreed terms which allowed supervisory co-operation so that host countries could be aware of products being sold in their Member States. With regard to business rules, it was agreed that the host Member States would take responsibility.

During the CEA discussions, it was evident that the UK contended that the continental system in general was too restrictive and anti-competitive. The main difficulties were:

(a) Prior approval of policies versus post notification checking.

(c) The maximum reserving rate of interest.

(d) The control of premium interest rate assumptions.

In these cases, the arguments indicated liberal and prescribed attitudes. The UK and its supporters pursued the more liberal objectives and the Germans and French, along with their supporters, a system of prescription and intervention. The creation of the insurance directives in general and the Third Life Assurance Directive in particular should not indicate winners and losers, but one where all Member States give and take to maximise their own and the consumers' positions within the newly evolving market. This is where the interest groups come into play: they are consulted on the proposed legislation and forward changes to the Commission. They are a pivotal entity with regard to the decision-making institutions and the insurance industry (for further see CEA Working Paper, 1990).

Through an interaction with the life insurance industry, during the early 1990s, the Commission was attempting to ". . . lay down rules for the exercise

of cross-frontier life assurance, balancing the needs of freedom to provide services and consumer protection and thereby developing the internal market in life assurance" (Commission Report, 1992; p 43). This is illustrated in the negotiations around the Third Life Assurance Directive and the accepted need for ". . . the co-ordination of laws, regulations and administrative provisions relating to direct life assurance" in the SEM (ibid, p 46). However, interaction is continually in process as the SEM in financial services is incrementally constructed.

The European Treaties outline the necessity of a single market in insurance if a true SEM is to be realised. The Rome Treaty emphasised that its objective was to create an internal market in the then European Community. This objective was outlined by, *inter alia,* Articles 52-59. These indicate the freedom of establishment and freedom of services.

In its proposal for the Third Life Assurance Directive, the Commission contended that the

> . . . completion of the internal market in insurance represents a primary goal of the Commission in view of the importance of this strongly expanding sector, particularly in life assurance, and the work already carried out in other financial services fields with regard to the creation of a single financial market (European Parliament Working Paper, 1992; pp 25-26).

Effectively, the Commission considered that the

> . . . European financial common market is an essential part of the frontier-free single European market, and encompasses not

only the free movement of money and capital for all citizens but also freedom of establishment and the freedom to provide cross-border services for brokers and financial undertakings. If the Community succeeds . . . Banks and insurance companies will be free to offer their financial products without restrictions . . . in all Community countries (European Documentation, 1989; p 5).

Thus, the financial common market was a cornerstone of the SEM programme.

Financial markets and particularly the life insurance market are highly regulated. Two reasons for this are to protect consumers from institutional failure and imprudent policies. However, ". . . sharing the same objectives does not mean that these are obtained by the same means and you will be aware that insurance legislation differs from country to country" (Drabbe, 1994; p 135)[3].

> The very specific nature of financial services is a . . . reason for particular difficulties in the integration of financial markets. In contrast to trade in goods, insurance and banking services in the individual Member States are strongly influenced by varying traditions of company supervision and investor and consumer protection (European Document, 1989; p 6).

"With regard to whether an SEM in life insurance is attainable the answer is yes. Even without the harmonisation of contract legislation the legal framework created by the directives gives the industry the opportunities to

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[3] Humbert Drabbe was head of the team that drew up the Third Life Assurance Directive. He was a key figure in DG XV.

realise it in practice" (Drabbe, 1994; p 141). Indeed, the EU has set up a Community filter to enable the protection of consumers on the one hand and competition on the other. The Community filter encompasses the need for restrictive practices to adhere not only to the 'general good' but to two further criteria as well. "Firstly, there should be no duplication of Member State rules or controls. And secondly, the same protection cannot be met through less restriction. Basically, it needs to meet a proportionality test" (ibid, pp 139-140). However, Drabbe pointed out that the difference in ". . . tax treatment of insurance products clearly raises major difficulties for a proper functioning of the single market" (ibid, p 141). If life insurance products can only be sold in a Member State if it 'qualifies', i.e. it ensures that policy-holders benefit from a favourable tax treatment, ". . . the tax regime effectively determines policy conditions and the marketability of assurance products. These have to be geared to the different tax requirements of each Member State . . . this is an infringement of the fundamental Treaty principles of free movement of persons and the free provision of services" (ibid). Harmonisation of tax bases and levels could overcome the problem (in principle at least). However, with taxation closely tied to the concept of sovereignty, it is unlikely that Member States would want to take this road in the short term. Yet it does point in the direction of closer ties in the area of financial services and indicate a spillover process. Initially, one may consider pragmatic solutions, where ". . . harmonisation is not a realistic option, a pragmatic answer could possibly be provided by ensuring that the tax authorities concerned receive the information necessary to draw up the tax form and collect the tax due" (ibid). However, further talks are still underway in this area.

By 1992, the specifics of the Third Life Assurance Directive were generally understood. Some considered it to be a "cultural revolution" (Loheac, 1992; p 2). Indeed, the Third Life Assurance Directive removes ". . . *a priori* control of

policy and rating conditions and replaces it with a non-systematic *a posteriori* communication system; this means that a long continental tradition of material control is abandoned and the essence of - which is attributed to the authorities of the country of the registered office - no longer focuses on the products . . . but the undertaking itself, its solvency, its shareholding and its management" (ibid, p 3). This should maximise competition in terms of products and increase innovation. However, there is a problem in terms of the 'general good' where Member State supervisory authorities may outlaw a product if it is deemed risky. Obviously, this allows the prescribed Member States a modicum of protection.

In general terms, the directive outlined a compromised framework which once in place relies on mutual recognition (given the concept of the general good). Once harmonisation has taken place, a form of confrontation will take place and

> . . . this confrontation with regulations should result in the different national rules being brought into line with each other: states which have a tradition of strict control will have to ease their regulatory constraints if they want to avoid penalising their own national undertakings . . . In the final analysis, the logical consequence would be that a less strict system of control would, in time, set the European standard (ibid).

This, of course, could only occur following an initial period of harmonisation or re-regulation. Effectively, the Commission saw the creation of the SEM as being pursued through three fundamental means; minimum harmonisation, mutual recognition and home country control. However, the:

> . . . principle of mutual recognition as a rule only applies to a list of activities generally annexed to the directives (either adopted or in the process of being so) in financial services . . . The approach by the Community authorities in directives on financial services is essentially institutional and sectoral. The specific features of each of these financial services sectors mean that they will be regulated by a body of formally and materially distinct regulations even though overall these texts are based on the same principles (adopted by the single licence) (Loheac, 1991; p 408 author's brackets).

Basically, in each specific sector there needs to be agreement on basic rules and these minimum harmonisation's are only possible because ". . . common interest, mutual confidence and a degree of economic convergence exist between EEC Member States" (ibid, p 409). It is on the agreement of this basic legislation that mutual recognition relies.

The liberalisation of the system should suit the UK life insurance industry and Loheac is correct when he notes that ". . . for British operators, an integrated European insurance market functioning on the basis of rules similar to the model they are used to . . . should be a favourable environment" (Loheac, 1992; p 4). However, although this may be the case, the UK would also need to make changes to its supervisory structure and the lack of contract legislation may negate any advantage. Finally, it was recognised that it was ". . . essential to overcome . . . differences in legal systems and regulations in individual Member States in order to create an integrated European insurance market" (ibid).

The Supervisors and the European Union

Also involved in the harmonisation process are the Member State supervisors. Russell (1988) considered that there were two issues to be looked at in the creation of the SEM. Firstly, regulatory concerns regarding the achievement of protection for the consumer and the investor; and secondly, the furtherance of market opportunities and the elimination of barriers to trade for the life insurance industry. These areas were problematic for all Member States. However, the UK attitude and philosophy is in most cases unlike the majority of Member States. The main difference between the UK and most of its partners revolves around the close supervision surrounding premium levels, policy conditions and permitted investments. The Department of Trade and Industry (DTI) felt that supervision to this extent reduced the scope with regard to competition, efficiency and choice.

In 1988, the need for harmonisation was admitted by the DTI. "On the one hand there is understandable pressure for a harmonisation of regulatory regimes and we are the odd man out among the European supervisors. On the other hand we believe that it is within the interest of our industry and European consumers that there should be more competition within Europe" (Russell, 1988; p 3)[4]. Russell was posing the question: how can it be ensured that the framework directive would allow the UK life insurance industry maximum opportunity when it competed in the SEM? "Many Member States have perfectly legitimate fears" (ibid) about a number of areas:

(a) how the freedom of trade would affect tax collection and the balance of payments;

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[4] Arthur Russell was the DTI representative involved in the formulation of the Third Life Assurance Directive.

(b) the effect freedom of trade will have on developing industries (they may be overwhelmed by freedom of competition).

However, the situation was that the financial services sector had lagged behind other harmonisation programmes in the EU. Indeed, ". . . progress in the common market is a question of bargaining, and we have to face the situation as it is not as we would like it to be" (ibid, p 6).

With the finalisation of the White Paper 'Completing the Internal Market' (1985) and the signing of the SEA, the Member States indicated their political will regarding the realisation of the SEM. Qualified Majority Voting (QMV) made it apparent that ". . . there must be a readiness to compromise. And to accept proposals which might be unpalatable if taken in isolation for the sake of a programme as a whole . . . No state can afford to be isolated, and needs allies . . . sufficient to block measures which they dislike. Often this can result in an unholy alliance where several states disagree on a particular proposal for many different reasons. And bridge building and trade-offs may often be necessary" (Russel, 1988; pp 7-8). Under the co-operation procedure set up by the SEA, decision-making became so much easier and a new impetus was given to the EU. However, the DTI undertakes its greatest participation in the process once the proposed legislation has entered the realms of the Council. "The DTI's main contribution is during the Council stage of negotiations where we send staff to participate in the working group . . . and brief the United Kingdom Permanent Representation . . . for COREPER discussions. The DTI depends on the BIIC for the views of the industry which interacts with the CEA and BIPAR to get an overall view of the European industry. They provide the DTI in the first place with industry's views on the overall shape of the directive and give invaluable assistance in resolving difficulties of a technical nature" (ibid, p 9). Clearly, interest groups are a very important

part of the decision-making process. They create areas of certainty, allow for the dissemination of information and encompass vehicles for compromise.

Conclusion

This chapter has overviewed the interaction between the insurance sector, interest groups and the supranational aspects of the EU decision-making institutions. However, it also recognises intergovernmental influences (e.g. the Council). Indeed, there is a tentative contention that multi-level governance processes may best describe the dynamics of European integration, recognising that multi-level governance shares both intergovernmental and neo-functional premises. In other words, both intergovernmental and neo-functional processes are at work in the formulation of European Union.

Finally, this chapter provided an overview of some recent interest group studies and recognised some of the difficulties in lobbying at the EU level. The most fundamental problem is the non-existence of a single decision-making body and that twelve (now fifteen) Member States have to be dealt with in the creation of policies and the uncertainty that this engenders. Interest groups that are involved in the policy process as representatives of a sector are a means of overcoming this. However, this chapter also recognises the intergovernmental aspects of interest groups, they ". . .must also take care not to neglect the national dimension of EC lobbying since the final decisions on policies are taken not by a directly elected European government, but by national officials and ministers" (Mazey and Richardson, 1993; pp 212-213).

The institutional inter-play involved in the formulation of the Third Life Assurance Directive provides an illustration of how a harmonisation process

is at work between the Member States. Each institution attempts to prioritise its understanding of what SEM legislation should entail. However, what is the overall process in terms of harmonisation and further integration? When do the individual Member States realise that they need to be part of the negotiations that create the legislation for the new market place? Do they realise that this is necessary? This and the previous chapter have indicated that there are different models of ideal legislation and regulation in separate Member States. We now question how these different ideals are compromised at the EU level? How far does self-interest give impetus to European integration?

Chapter Seven

Decision-Making Models and Processes of Integration: The Interview Programme

> *I am European, I am no doubt a European intellectual, and I like to recall this to myself, and why would I deny it? In the name of what? But I am not nor do I feel European in every part that is European through and through (Derrida, 1992; p 82).*

Introduction

In Chapter Five we examined the different understandings of regulatory environments that Member States hold. The survey indicates the amount of regulation a Member State would feel most acceptable and the demands it would make to ensure its interests. Chapter Six discussed and illustrated the different groups influencing the EU decision-making process; and this chapter builds an understanding of how the different positions (regarding regulatory environments) are compromised by the Member States at the European level. To do this and to indicate how the actions of sectors/companies are influential in the process, the analysis uses:

(a) An amended 'demand flow' model. This suggests how interests transfer into demands and how these demands are channelled into decisions (Easton 1965, see Fig 7.1 p 214).

(b) A European Demand Model which clarifies this process at the EU and Member State level (see Fig 7.2 p 215).

(c) A decision-making model derived empirically through interviews with representatives of EU and Member State level decision-makers (The European Decision-Making Model Fig 7.3 p 243).
(d) A Survey of UK life insurance companies.

The thesis considers that there is an interaction between economic sectors and political institutions in the decision-making process and that such an interaction may be located in the processes apparent at the EU level. This process is evident in the life insurance sector because of the amount of differing legislation and the consequent difficulty in establishing an SEM. This provides an example of supranationalism in the integration process. Overall, through the interaction between interest groups and the EU certainty and clarity are provided. The ground rules are indicated and the parameters of policy formulated. However, in the context of supranationalism just

> . . . as the European Community is itself still developing its institutions and policies, so the interest group system surrounding the EC has yet to reach a stable state. We are still in the relatively early stages of group adjustment to a shift in the locus of power and it, therefore, is not surprising that the process of interest group intermediation is in a state of flux (ibid, p 213).

Building on the process outlined in the previous chapter, this chapter, questions the extent of the flux and locates the process in a theoretical framework.

Easton's Demand Flow Model

David Easton (1965) developed a general model of how institutions may channel conflicts into merged ideological patterns. Indeed, this thesis posits a number of scenarios based on the Easton model. For Easton there are a number of demands on the political system and he considered that ". . . conflicts over demands constitute the flesh and blood of all political systems from the smallest to the largest, from the simplest to the most complex" (Easton, 1965; p 48).

In his model, Easton illustrates how *expectations, public opinion, motivations, ideologies, interests* and *preferences* transfer into wants which become system inputs. With reference to the life insurance industry and the EU, one may consider that there is an over-riding ideology indicated by socio-historic circumstances out of which the other variables emanate; thus ideology takes the form of Member State understanding of the amount of regulation that is necessary for their environment, i.e. totally free, prescribed, state controlled. Interests may be viewed as a Member State's most desired point in relation to the specific environments, the most favoured conditions. This illustrates the need for interest groups at a European and national level because they are the most appropriate vehicles to enable compromise. Preferences are linked closely to both ideology and interests and denote those areas most likely to be accepted (the extent of compromise). Motivations include the need to be involved in the discussion process to ensure legislation as close to one's desired position as possible so as not to undermine trading capabilities (to allow for profit maximisation and certainty). These variables are subsequently transferred into demands.

Demands effectively threaten the system and have to be dealt with. Indeed, any surviving system must have created the means by which demands from different parts of the system can be resolved. Easton (1965) considers that there is a general sequence that deals with the stress that demands create:

Stimulus > System > Response > Outcome.

Demands create a disturbance or stimulus and the system feels the effects; system members respond or fail to respond; the result or outcome reveals how well the system has coped with the stress created by the disturbance. Without demands, the system would not know which decisions to make, as it would be unaware of interests.

Consequently, demands are central to Easton's model as they constitute an expression of opinion that forces the decision-making body to deal with the problem. Easton considers that demands may be:

(a) Specific.

(b) Generalised.

(c) Ideological (a set of demands).

These demands are always directed toward the authoritative body (in this case the EU institutions) to take the desired action (one would consider that this held preferences). Effectively, Easton considers that all demands are the same; only the directions are different i.e. those that push for desired action and those that do not.

Easton defines interests as the means by which a person or group attempts to implement fundamental goals. In such a way a law or policy could be said to be made in a person's or group's interest, the realisation of the interest fulfilling a basic goal. Indeed, ". . . interests might easily be confused with demands. However close a connection there may be between the two, it is important to recognise that conceptually, they are quite separate" (Easton, 1965; p 45). He emphasises this point through delineating interests into categories, i.e. subjective and objective interests.

Subjective and Objective Interests

Easton defines interests as:

> . . . instrumental values, those means through which a person or group seeks to implement what may be considered to be his or its fundamental goals. In this sense, a person may speak of a law or administrative decree or policy as being in his interest . . . In this instrumental sense, we may describe interest as either subjective or objective (ibid).

A subjective interest is one where one's own interpretation of what is necessary is paramount, if broader goals are to be recognised. In this context, the analysis will investigate how fundamentally desirable interests of European Member State life insurance industries are met and compromised to ensure desirable system changes, i.e. the move from a national market to cross-border trade.

> From the subjective point of view, the interest of a person is to be found in his own interpretation of what is necessary if he is to

> realise his broader goals. . . . More usually, in politics, subjective interests would be attributed to groups, as where they are perceived and voiced by an organisation that presumes to speak for its membership at the very least (Easton, 1965; p 45).

An objective interest could specify criteria that has no regard for the interests of the industry. "An objective interest may be described as those instrumental needs which others attribute to a person or group according to criteria quite independent of the subjective perceptions of that person or group" (ibid).

Easton illustrates the difference between objective and subjective interests; the interviews in the thesis attempt to identify the insurance industry's subjective interests in relation to the objective interests of the EU. A subjective interest is one which the industry recognises itself and interprets what is necessary if broader goals are to be achieved.

A subjective interest becomes a demand if it is not met; an objective interest becomes a demand if it is not what the industry requires (some of the difficulties regarding this are illustrated in the previous chapter). In this context interaction between the conflicting areas is necessary.

Chapter Five identified subjective interests and Chapter Six and Seven explore how subjective interests are agreed upon? Who voices the interests? And how do these interests transform into demands? An objective interest may be described as others interpreting the interests of the group. Such an interest would take into consideration external needs that ensure the goal i.e. the regulatory environment. In respect of the life insurance industry, this would take into consideration cross-border trade and the long term effects of this on the life insurance industry. At this juncture one would be forced to

ask from where an objective interest would obtain the information of what is necessary for the industry's survival? And how happy would the industry be in leaving its fate in Europe to objective interests? However, as Easton indicated, ". . . the expression of an interest in a matter is not identical with the input of a demand. To become a demand, there needs to be voiced a proposal that authoritative action be taken with regard to it" (ibid, p 47).

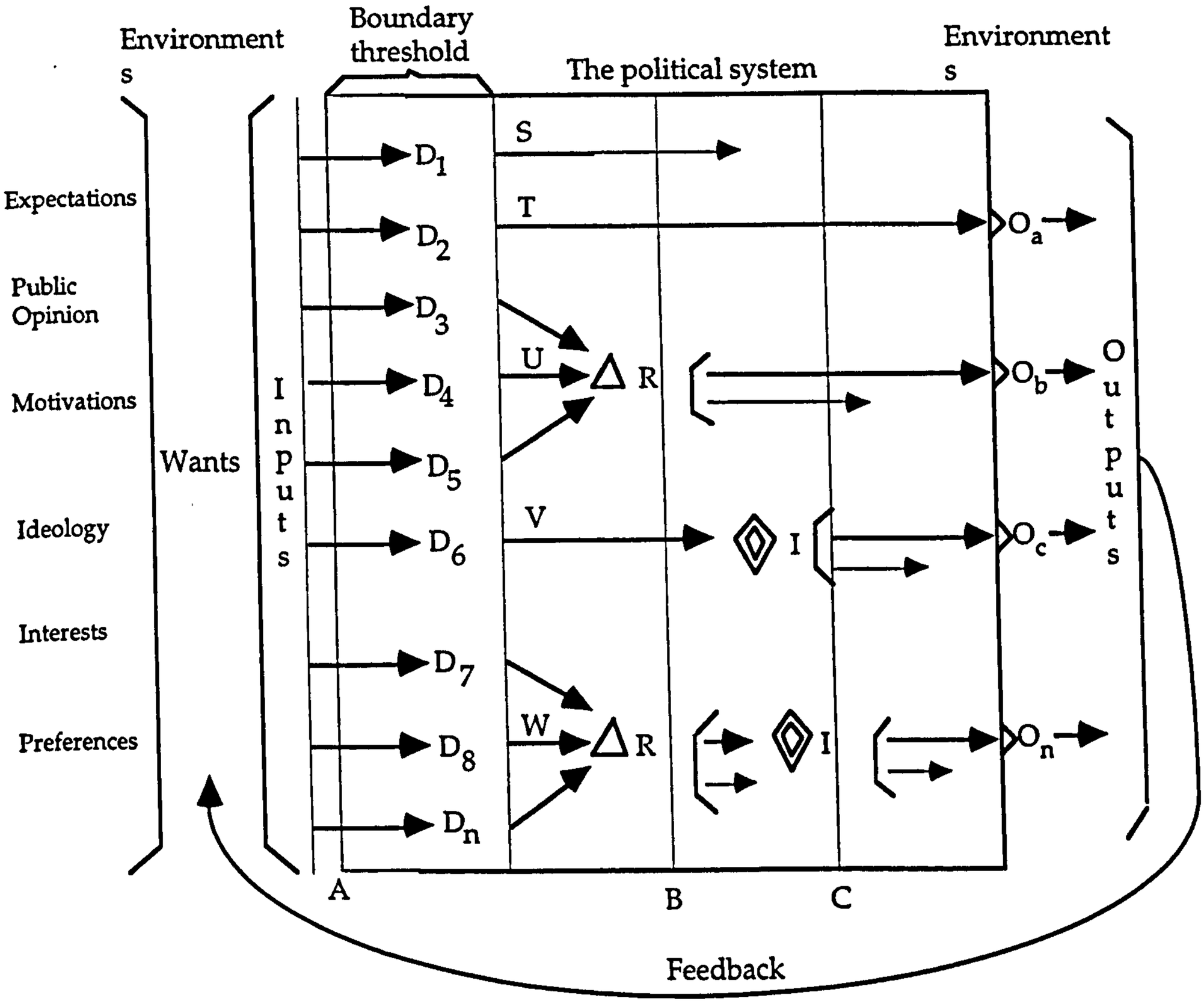
An Applied Demand Flow Model

In a post-SEA Europe, the decision makers at the EU level have become much more prominent in Easton's system change and system insurance processes. When changes are to be made at the EU level, are subjective interests (the interests of the life insurance industry) brought to the attention of the national legislature which subsequently relays them to the European decision-making institutions? If this were the case, would the national legislature relay these interests to the European level with its own objective interests added to those of the life insurance industry's interests? Or would the life insurance sector relay its own subjective interests directly to the European decision-making institutions which would have their own subjective interests? Fundamentally, how and in what form (objective/subjective) are the interests brought to the attention of the European and national decision-making institutions and formulated into demands? This thesis considers that subjective interests are formulated at the national level through the national companies and national interest groups. These interests are formulated further at the European level and interact with the objective interests of the EU to create European legislation. However, not all interests become demands. "Whether we accept a subjective or objective interpretation of interests or recognise them as mutually compatible ways of delineating and classifying interests, my point is that we cannot automatically

conclude either that interests are synonymous with demands or that every interest must become incorporated into a demand (ibid, p 46).

This thesis applies Easton's model to the EU which (see Fig 7.1 p 214) allows an understanding of what takes place between the different European institutions (Commission, Parliament and Council), interest groups and insurance companies. One may contend that interest group-Commission-Parliament interaction takes place between points A and B; Commission-Parliament-Council interaction between points B and C; and from point C on the members of the Council negotiate the end result. This is best illustrated by inputs D7, D8 and Dn = W. The different Member State demands are compromised at point R following interaction between national interest groups at the European level, this involves Parliament and the Commission; while interaction between the Commission, Council and Parliament is affected between B and C. Finally, legislation is agreed at the Council level, or between C and outputs. These outputs revert to wants and demands and illustrate the spillover process. With regard to the rest of the model: S is a failed piece of legislation, T is uncontroversial and does not necessitate compromise, U illustrates different demands but the process following a compromise (at point R) does not illustrate the EU in general terms (because it does not provide for the interactions between the European institutions). V illustrates only one demand.

FIG 7.1 **EASTON'S DEMAND FLOW MODEL**



D_1 - D_n Voicing of demands.

→ Flow channels and patterns.

→

△ R Reduction and combining of points.

◇ I Conversion to issues - demands transformed into issues.

O_a - O_n Conversion to outputs.

Feedback - Although this is only one line it represents numerous feedback channels.

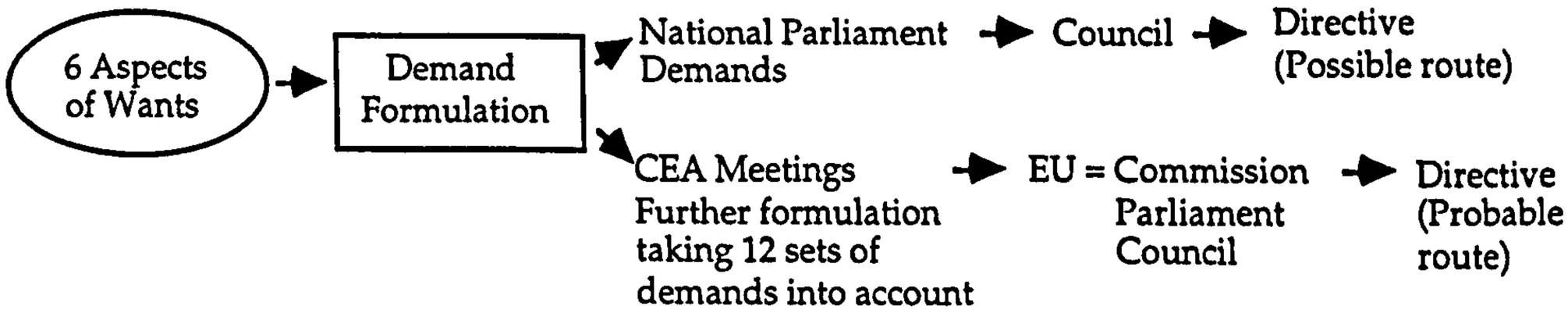
(EASTON, 1965; pp 74-75)

Ultimately, one may consider that demands are fed into the system by the companies, either straight to legislatures, or they are channelled by interest groups.

This thesis concentrates on the European side and claims that demands in respect of European needs are formulated at Member State and European interest group levels. Easton's adapted flow model considers that at the EU level, a compromise is reached between the Member State life insurance industries while an interaction takes place with EU institutions. Of course, other routes may be taken, as is illustrated in the European Demand Model, Fig 7. 2. The investigation intends to clarify this process.

FIG 7.2

THE EUROPEAN DEMAND MODEL



The European Demand Model (Fig 7.2) provides a bridge between Easton's adapted Flow Model (Fig 7.1) and the European Decision-Making Model (Fig 7.3 p 243). The Demand Model attempts to assess the decision-making routes taken by the Member State life insurance industry once legislation for their sector has been proposed. The European Decision-Making Model (Fig 7.3) is

initially grounded out of the previous two models, then added to and constructed further through the interview programme.

The emphasis on the European dimension intensifies as integration gathers pace and the need to be involved at the European level becomes increasingly apparent. The growth in the number of interest groups and lobbying bodies between direct elections in 1979 and the SEM in 1992 seems to indicate this, as does the growth in the post-SEA era.

There are a number of insurance interest groups at the EU level the most important of which is the CEA. At this point both Member State interest groups and insurance companies consider national differences and attempt to reach compromise positions in respect of national ideologies, interests, preferences etc.

Regarding these problems, the areas that need investigation are:

(1) How does the national/European life insurance industry recognise its subjective interests with specific reference to the SEM?

(2) Do these interests transfer into demands and how are these demands made of the national or European legislatures?

To enable some answers to these questions, there are five areas that may be investigated and each engenders a certain route that demands may take. These are:

(a) National industries make demands of national legislatures prior to formulation at the European level.

(b) The formulation of demands between national interest groups are compromised between Member State insurance industries at the European level then made of the European and national legislatures.

(c) Companies or national interest groups make demands of their national legislatures which make decisions and without further consultation transpose these to the European legislature.

(d) The national legislatures formulate the requirements of the industry without consultation.

(e) The European legislature formulates market legislation without consultation.

A number of these questions were investigated by Mazey and Richardson (1996) who interviewed more than forty Commission officials and surveyed fifty officials from a number of DGs. Indeed, ". . . it was clear that officials placed enormous importance on the consultation of interest groups, typical responses were: I see consultation as an important and very useful source of information to ensure that EC legislative measures are efficient and effective in the real world (Dutch Official DG XV). We strongly value open, extensive and continuing consultation, formal and informal - our whole activity is based on this (British official DG XII). Consultation is in general positive as it allows us to broaden the perspective on a given-issue (Spanish official DG XVII)" (p 201).

The above questions were investigated in the interviews that were undertaken with individuals involved in the formulation of the Third Life

Assurance Directive. Each of the five strategies necessitates different routes in the decision-making process and these may differ among the Member States. However, a specific model may be posited, different routes illustrated and the most rational strategy indicated.

The Interview Process

Through a series of interviews with EU decision-making bodies this chapter provides an investigation of where interest groups predominantly level their demands, and how they are dealt with by EU institutions.

The survey data illustrated the way the life insurance sector perceives the EU and how it attempts to mould a future regulatory environment (Life Insurance Regulation Matrices One and Two, pp 157 and 160). These ideological preferences are provided by different cultural existence. The decision-making process in the EU and the regulatory environment to be formed through such a process may tell us much about the way future trading in the EU may develop.

Interviews were undertaken with a number of key individuals concerned in the decision-making process at the European level. The interviews at the both the EU and UK level provide information that may allow the thesis to deduce a similar process among all Member States. Interview outlines (see p 221 and Appendix B) and survey B (see Appendix A) were sent to other Member State interest groups and the responses allow some deduction of processes at work throughout the EU.

The key individuals who were personally interviewed by the author were representatives from the following institutions.

Directorate-Generale XV. (DG XV) (Finance). M. De Frutos. 12-30 pm 11 September, 1993, DG XV, Brussels;

The Council Permanent Representative for UK in Finance. Mr R. Quinn. 11.00 am 6 August, 1993, 6 Round Point, Robert Schuman, Brussels;

The Department of Industry & Trade (DTI). Mr M. Ingram. 2.30 pm 22 July, 1996, 1 Victoria St, Westminster, London;

Committee for European Assurance (CEA). M. Binon, 10.00 am 14 September, 1993. Rue Belliard, 9. Brussels. Herr Werle 2.30 pm 23 February, 1996. Paris;

Bureau International des Producteurs d'Assurance & de Reassurance (BIPAR). Herr H. Krauss, 11.00 am 8 September, 1993. Avenue Albert Elizabeth, 40 Brussels;

Association of British Insurers (ABI). Ms J. Frost 2.30 pm 17 May 1996. 51, Gresham St, London.

British Insurers International Committee (BIIC) Mr A. O' Leary 2.30 pm 7 August 1995 (home address) Cheltenham.

Interview outlines (as indicated in Appendix B) were returned by the:

Irish Insurance Federation (IIF). Mr J. White;

Council Permanent Representative for France. (Attache financier). P. Charlier.

Each interviewee was an individual who dealt explicitly with the Third Life Assurance Directive and each illustrated interaction with others. The questions were codified so that each set of interview questions related to each other. This allowed a general perspective of the EU decision-making process and illustrated the interactions between the key players.

Formulating and Coding Semi-Formal Interview Questions

Grounded theory entails two basic analytical procedures. Firstly, one continually makes comparisons and secondly one asks questions. As noted above these processes have been adhered to in earlier parts of the study. However, at this point the study wishes to identify the process in relation to the interviews. Questioning opens up the data and through using the categories properties and dimensions constructed earlier in the study the researcher is able to ask precise and revealing questions in the interviews. There are general questions that can be drawn from the data which can stimulate a series of questions which in turn ". . . lead to the development of further categories, properties and dimensions. The basic questions are **Who? When? Where? What? How? How Much? and Why?**" (Strauss and Corbin, 1990; p 77). The interview questions (see below p 221) build on the basic questions and the previous categories that were generated above. Indeed, the difficulties that were created through the categorisation of the European life insurance industry provide the basis and strategy of the interview questions. They *emerge* to deal with the problems and contradictions that the study has uncovered.

The interviews were conducted on a semi-formal basis and centred around 12 core questions these were;

(1) What are the major functions of the CEA/BIPAR/ABI/the Commission/the Council/National Supervisors and how do these fit with each other at;
(A) The EU level.
(B) The national level.
(2) To what extent are decisions made with interest group/COREPER/Commission/National Supervisor in-put.
(3) Is it interest groups, national supervisors, the Council of Ministers or the Commission that define decision parameters.
(4) Does the Council, the Commission, national legislatures and interest groups reach a compromise prior to a decision reaching the Council.
(5) Does an interaction exist between the Council/the Commission/national supervisors and specific interest groups at a national and European level.
(6) How does the Council/national supervisor know what to insist upon in respect of national interest.
(7) Does an interaction exist between interest groups/Commission/Council/national supervisor and the Insurance Committee
(8) Are different Member States looking for specific types of life insurance regulatory environments for the SEM which is different from other member states.
(9) Are there differences between the;
(a) The French ideal
(b) The German ideal
(c) The Dutch ideal
(d) The UK ideal
(e) The Italian ideal
Please illustrate these differences.
How does your market ideal fit into these?
(10) Is a compromise reached between the different national interest groups prior to the Commission initially drawing up draft legislation or is there an interaction between the interest group at the European level and the Commission which takes into consideration a compromise reached by the Member State interest groups e.g. ABI through membership of the European interest group CEA/BIPAR.
(11) Where possible have compromises been reached between the Council, the Commission and Parliament before the final negotiations to enable a more efficient means of decision making?
(12) What takes precedence in the formulation of a directive Member State or sector interests?

The questions were coded into categories so the same could be asked of each interviewee. This allowed the following categories to emerge from the interviews: **Understanding; Negotiation; Interaction; Difference; and Compromise** (see the interview results below).

The Interview Results

In general, the interviews indicated agreement on a number of points. The Third Life Assurance Directive was unanimously perceived as a means of providing the environment that would allow mutual recognition to be achieved; it was also acknowledged that many influences went into the drafting of a directive. Since 1988 interaction between industries and the Commission has become more apparent at the EU level. The representative of DG XV considered that consistent contact with the life insurance industry was imperative in respect of legislative input.

Question One ***(Understanding)***

What are the major functions of the Permanent Representative/Commission/CEA/BIPAR/ABI/DTI and how do these fit in with the functions of other finance interest groups and governmental institutions at:

(A) The EU level?

(B) The national level?

The Directorate General XV deals primarily with the CEA and BIPAR. However, the impetus for legislation may come through the Member States or from the Commission itself. The CEA sees its **role** as bringing together a

combined understanding of the direction negotiations should take. The CEA, BIPAR and DG XV representatives all considered that the Commission prefers to deal with a European-wide interest group. Both the ABI and BIIC agreed with this view and thought that the ABI and BIIC worked through the CEA as these days (post-SEA) it was easier to get **unanimous** views in the latter organisation. This they felt was due to the general acceptance of the UK's understanding of a regulatory structure, but this was disputed by other interviewees and survey A. Initially, the European life insurance industry was divided but through the integration process and the recognition of the necessity of a **united front**, a more compromisory situation is now sought. Consequently, the importance of the CEA has continued to grow. This allows for negotiations to be more specific because individual company and national interest group involvement creates too much information and creates the difficulty of turbulence. Turbulence is the concept initiated by Haas which posited that in the integration process there is too much information which serves only to cloud the situation (Haas 1976). In this context, interest groups in general and European interest groups in particular create **wholes** that enable **shared belief systems** and **focal points** that define, for those, involved what constitutes co-operation (Haas, 1975; Garrett and Weingast, 1993).

Additionally, the BIIC also **communicates** with the national government through the Department of Trade and Industry (DTI). This ensures that proposed legislation is acceptable to all of the parties concerned and successful at the Council level. Once the Commission and the industry are committed to a policy approach, the BIIC supports it with information and attempts to prevent backtracking (BIIC Representative). The ABI and the IIF do the same work as the CEA at the national level. In this context, the ABI through the BIIC interacts with the DTI on a regular basis to **ensure that government fully understands** what the industry needs. However, the DTI did point out that

although it was also interested in the needs of the consumer, in general terms the understanding of the insurance directorate is developed through the industry. At the EU level, the DTI is involved in Council working groups and gets involved in **bilateral discussions** on an ad hoc basis in an attempt to swing other Member States toward the UK's stance. The **discussions** pave the way for some kind of **consensus** in the working group. In this context, more of an intergovernmental perspective may be observed. However, this would incorporate **"advice received from the industry"** (DTI Representative) through the use of interest groups. The BIIC ". . . advises . . . on a regular basis and as the BIIC meeting precede the Council working group by two weeks, we go in broadly knowing what the industry wanted" (ibid). The IIF represented the Irish life insurance industry's interests at the EU level through **lobbying.** It would also have regard for other finance interest groups: these may be seen as allies or competitors. However, through the CEA **compromise** is usually reached. This illustrates more of a neo-functional rather than an intergovernmental perspective.

Questions Two and Three ***(Negotiation)***

To what extent are decisions made with interest group/Commission/Permanent Representative/DTI input?

Is it national/European interest groups, national supervisors the Council Ministers or the Commission that define decision parameters?

The Commission looks towards creating a **common understanding** between the Member States. It will **interact** with Member State interest groups, e.g. the ABI or even directly with companies. But its main contacts are the European interest groups because they allow a **European perspective** and this is what

the Commission wants (this was substantiated by the European interest group representatives). In this context, the CEA has little to do with national governments, leaving this area to national interest groups. As well as **attempting to influence** in this area, national interest groups will hold **direct talks** with Commission representatives occasionally, but usually through European interest groups. National interest groups deal with MEPs at the European level. The IIF representative considered that **"generally interest group input is taken fully on board"** (IIF Representative). However, interest group input is not the sole factor.

The creation of a **consensus** between Member States allows for **successful legislation** when it reaches the Council because it has been partially agreed in the initial stages. Of course, problems may occur once **negotiations** take place in the Council. However, **successful legislation** may be more apparent if there has been **agreement in the initial stages.** This was substantiated by the DTI representative.

The CEA representatives both considered that the CEA played an **interactive** part in the **creation of European legislation,** as did those representatives of the ABI, BIIC and BIPAR with reference to these organisations. Parameters in terms of decision-making are created through this process.

There are many influences built into a proposal:

(a) The **individuals in control,** e.g. Delors, Brittan.

(b) The **institutions in control,** e.g. the Commission, Court of Justice, Parliament, Council.

(c) The **economic sectors' perceptions** of the legislation necessary.

However, it is the economic sectors that act as a **stimulus and interact** with the European political institutions. There is much **input** by trade associations who look to make their **influence** felt as early as possible. In this respect, the insurance interest groups interact with the Commission at the following five levels of proposal formulation:

(1) The **forming** and **influencing** of ideas.

(2) **Discussing** the general problem.

(3) Having an **input** into draft working papers.

(4) Having an **input** into formal proposals.

(5) **Lobbying** Commission **discussions.**

(These levels were indicated by DG XV, CEA and BIPAR Representatives)

Theoretically, by level 5, the 'Commission discussions', **agreement** should have been reached. However, there could be minor disputes. At this point the **proposed legislation** is passed on to the European Parliament which gives its opinion as it would also have been lobbied by the given groups. Recently, (1996) the **"European Parliament invited CEA representatives along with seven other large European interest groups to indicate that it would like to deal specifically with them rather than the large number of bodies that currently attempt to lobby it"** (CEA Representative).

It was thought by the Council representative (UK Permanent Representative) very likely that the Council would **support** the major areas of proposals. However in some cases, it would not. Proposed legislation does not always totally reflect an **industry's opinion** in the way that the Commission's representative implied (DG XV Representative). However, **legislation is easier to implement with consensus:** yet if this is not possible, the proposal is still constructed. If the proposal is constructed without **general consensus** of

the sector, **implementation** becomes much more difficult and in some cases impossible. The insurance contract directive was a case in point that was taken up by the DG representative in relation to this area. This was mirrored by the French Permanent Representative, who considered that interest group **input** into the decision-making process was high and of an interactive nature. The role of the COREPER is to provide **consensus** and the **greater agreement** there is prior to their involvement, the easier their role becomes.

The BIIC representatives thought that interest groups were extremely **influential** in the building of legislation and that this helps in the **initiation** successful legislation. O'Leary considered that the Commission was very **open** but had no programme: it also had to face a division of opinion throughout the EU. Interest groups at the European level have helped to overcome these divisions. Frost considered that the trend these days was to seek **compromises**. However, in some cases Member States were reluctant to shift away from their preferred regulatory system, but she added that the UK has and will continue to shift when necessary.

Ultimately, the CEA is a **pivotal body** that allows an all-round or **complete perspective** of the sector's demands for the decision-making bodies. There was an increase in CEA activity in the mid-eighties following the Commission White Paper (1985) and the SEA which indicated the creation of the SEM. The CEA sees itself as a **facilitator** and a **negotiator** of turbulence (as indicated by Haas 1975). European interest groups provide the means for an all-round European view and this allows for more **successful legislation** (CEA Representative).

Consumer product protection is provided by contract law. However, this is an area where harmonisation has proved difficult to achieve and allows an

illustration of the difficulties involved in harmonisation when areas more sensitive to national sovereignty are broached. After fourteen years the insurance contract directive proved impossible to agree and finally it was abandoned. This does not provide the environment necessary to allow a SEM in life products because a Member State can theoretically block a product from crossing its border. De Frutos pointed out that a host country could not impose regulations in a "willy nilly" manner but only in the context of the 'general good'. Of course, one has to determine what is meant by this concept as it is open to a number of interpretations. One Member State's 'general good' providing another's trade barrier. However, De Frutos indicated that the Commission was continuing to monitor the situation.

It was apparent that it had been difficult to get agreement on the simplest parts of the insurance contracts directive. This gives an understanding of the problems the EU has if it does not undertake **consultation** with industries and interest groups. If it presses ahead alone difficulties are likely to be apparent at the Council level. A high level of **consensus** is necessary if proposals are to become legislation. It also illustrates the situation when the EU **interferes** with areas fundamental to the idea of **Member State sovereignty** e.g. contract law in general, taxation or pensions, etc. When the EU attempts **interference** in such areas it is effectively tampering with civil systems and this ruffles the nationalist feathers (for a further discussion see Chapter Five and the Spillover Model, Figs 5.1, 5.2 and 5.3 pp 277-81).

In general, decision parameters are defined by different organisations at different times during the creation of the legislation. The national interest group **informs** national government what the national industry needs. However, these needs are curtailed by other Member State industries and it is here that the European interest group comes into play. The Commission

initiates the legislative process but needs the **inputs** of the interest groups to engender successful legislation. It must also remain loyal to the spirit of the treaty. Ultimately, the Council may amend a proposal as long as the vote is unanimous.

Each organisation is involved in **defining decision parameters** because without the input of each Member State, the insurance industry and EU institutions legislation would not hold the **essential ingredients** to ensure its **successful passage.** This was emphasised by the French Permanent Representative who considered that **interest groups define decision parameters** regarding their area of interest. However, this is not the **general interest** and this is where the **Commission and the Council provide a balance.** The Council provide parameters once the legislation has reached them ". . . at the general level and often negotiate precise texts for validation" (French Permanent Representative) but it is the Commission that has the "power of proposition and objection" (ibid).

The **ideal is consensus.** However, this is difficult to achieve without fundamental changes to the decision-making structures and an undermining of national sovereignty in the areas of legal structure and fiscal and monetary policy. 'General good or best practice' may be a means toward enabling this. Werle contended that on a number of occasions agreement has not been reached by Member States and in these cases 'best practice' is brought into play. At the interest group level, they pursue **unanimity:** however this is always difficult and in some cases impossible.

In principle, the Commission defines the **decision-making parameters.** However, as illustrated above, one may argue that it does not do this alone. Because the Council provides the decisions it could be said that it is this

institution that provides the parameters. Additionally, if one takes into consideration interest group **input**, one may consider that these define parameters prior to the involvement of any institution or through an interaction with the Commission. Werle commented on the role that the CEA played in the European decision-making process. **"The Commission provides a framework for the CEA. Then the CEA undertakes negotiations with its membership"** (CEA Representative).

Questions Four, Five, Six and Seven ***(Interaction)***

Did the Commission/Council/Parliament, national legislatures and interest groups interact and reach a compromise prior to the Third Life Assurance Directive proposal reaching the Council?

Does an interaction exist between the Commission/Council/Parliament and the specific interest group on a national (ABI) and/or European level (CEA)?

How does the Commission/Council/Parliament know what to insist upon in respect of European interests i.e. in terms of insurance policy that is acceptable to all Member States?

Does an interaction exist between Permanent Representatives, interest groups, the DTI and DG XV? Is this interaction undertaken through the Insurance Committee (if so how effective is the Insurance Committee)?

There is an **interaction** between the European and national institutions; the Council and Commission have college meetings where **policy lines** and **strategies** to pursue these **policy lines** are decided. Parliamentary **opinions** and assent are taken into consideration with a greater importance given to these

since the Maastricht Treaty. However, this was minimal in respect of the Third Life Assurance Directive. As stated above, the Commission and Council acknowledged that there was an **interaction** with interest groups on a European and national level. Indeed, that the Commission would primarily go to European interest groups because such would provide an **overall picture** of the industry. The UK Permanent Representative considered that the Council does not really deal with interest groups directly but CEA papers are forwarded to both it and the insurance committee. Whereas, the French Permanent Representative considered that they ". . . have contact with representatives of specific interest groups when there is a need of information" (ibid). Of course, this could be similar to the UK position or more informal. However, the French Permanent Representative was quite clear on the extent of **compromise** between the different groups before decisions reach the Council. To the question, ". . . do the Council, the Commission, national legislatures and interest groups reach a **compromise** prior to a decision reaching the Council" the French Permanent Representative answered ". . . yes, this is always the informal rule of procedure".

De Frutos contended that DG XV knew what to insist upon in respect of what was necessary for a proposal by examining the green papers and treaties. However, he did admit that **input** from the specific industry or sector had to be seriously considered.

The representatives of the ABI/BIIC considered that normally the Council, Commission, national legislatures and interest groups reach a **compromise** prior to the legislation reaching the Council. It is unusual for something to reach the Council without a **compromise** being agreed (ABI Representative). The BIIC representative considered that the **consensus** view was created by

the Commission with the use of interest group **input**. However, there is no **interaction** between the Council and the national interest group. In this context, **lobbying** is undertaken through the DTI. It is through this process that the Council **identifies** what the national industries will accept or need and the DTI is always willing to speak to national interest groups but they may also have their own agenda (but they know what is needed because they talk to interest groups).

It was generally agreed that the CEA and BIPAR both illustrate points where European compromises may be met which allows an easy **interaction** between the Commission, the Council, and Member States. Decision parameters are built up through **four interacting areas:**

(a) The **Treaties' aims.**

(b) The **European institutions** (i.e. through college meetings and decision-making procedures).

(c) Member States.

(d) Industries (interest groups and companies).

An indication of the need for **interest group interaction** is exemplified in the formation of the Insurance Committee Directive (91/675/EEC). This has allowed an expertise at the Commission level to ensure that there is an **understanding** between the industry and the Commission with reference to technical issues. The Insurance Committee is a new phenomenon which is being used to greater effect at an increasing rate.

The ABI/BIIC does **interact** with the insurance committee, as does the CEA. The Committee allows problems to be discussed and overcomes difficulties with **interpretation.**

In this context, the EU institutions find the committee helpful. It also makes technical adjustments to financial instruments and provides a **sounding board** for the Commission (ABI Representative). However, the French Permanent Representative considered that although such a process did exist the **interaction was one of an informal nature,** i.e. through professional contact.

*Questions Eight and Nine (**Difference**)*

Were different Member States looking for specific types of life insurance market environments for the Single European Market (SEM) which were different from other Member States? (Could you indicate these differences, please).

Are there set parameters from which the Commission/Council should not stray in the decision-making process? (Could you indicate how these are reached ,please).

In general, each interviewee agreed that different Member State industries wished the EU to create **conflicting** regulatory environments. Werle contended that there were **different** concepts of what a regulatory environment entailed between the Member States and that this was due to **differing** normative and historical **experiences.** If it was accepted that there were **different** understandings of regulatory environments, it was agreed that European-wide interest groups were necessary to bring about consensus. He

saw the necessity of best practice and how mutual recognition may overcome this. However, he agreed that a lack of contract legislation could undermine an SEM in life insurance.

The BIIC representatives agreed that there were **different** concepts of the regulatory environment in terms of products, cultural norms, technical and product barriers. Each indicated that there were **market ideals** pursued by **different** Member States: these were agreed in general by all those interviewed:

French Ideal = **Nationalised/Prescribed.**

German Ideal = **Prescribed.**

Dutch Ideal = **Liberal.**

UK Ideal = **Liberal.**

Italian Ideal = **Prescribed/Liberal.**

Eire Ideal = **Liberal/Prescribed.**

The **individual** regulatory environments were considered to be very **different** from one another and as the Life Insurance Regulation Matrices One and Two illustrated (see Figs 5.1 and 5.2 pp 157 and 160), each accepted that some form of **compromise** had to be reached if **harmonisation** was to be successful.

Questions Ten, Eleven and Twelve ***(Compromise)***

Is a compromise reached between the different national interest groups prior to the Commission initially drawing up draft legislation or is there an interaction between the interest group at the European level, i.e. CEA and the Commission, which takes into consideration a compromise reached by the

Member State interest groups i.e. ABI through membership of the European interest group?

Where possible have compromises been reached between the Council, the Commission and Parliament before the final negotiations? Would this allow a more efficient means of decision-making?

What took precedence in the formulation of the Third Life Assurance Directive, Member State, European (Commission) or life insurance industry interests?

To ensure successful legislation, **compromise** between these areas needs to be reached. Consequently this is pursued before the **final negotiations** to enable more efficient decision-making. **"Compromises are achieved through working parties where agreements are reached and Member State and interest group policy lines merged"** (UK Permanent Representative). **"It occurs sometimes especially when there is a European organisation for a profession"** (French Permanent Representative). **However, ". . . the Commission never loses sight of the spirit of the proposal"** (DG XV Representative). **"Compromises are reached through IIF involvement in a European interest group"** (IIF Representative).

The formulation of the proposal and consequent directive must take into consideration all **input**. However, precedence of **input** is difficult to distinguish. The Commission, as noted, concentrates on the **"spirit of the Treaty"** (DG XV Representative) or the EU interest; to do this it must take on board **national interests** and **industries' interests** and minimise the difference to ensure passage through the Council. This, one may argue, can only be

achieved through the use of interest groups and more importantly **European-wide interest groups.**

In a post-SEA Europe, industry in general has recognised that it is in their **interest** to have an input into forging the new market and have **co-operated** because they consider the SEM acceptable. Pre-1988, there was a **conflict** between the EU and industry: effectively, they seemed to be in **opposition.** It was the SEA that gave the impetus to the SEM which forced the Member State industries to be involved in the **formulation** of their evolving home market.

Interest groups became more aware of what was necessary for creating European Union in a post-1986 scenario. Of course, there are a number of difficulties in attaining **agreement** continually and Member State interest groups and companies will continually attempt to **influence** the decision-making bodies themselves. However, the European decision-making bodies make it clear that negotiations should be undertaken through the CEA or other European interest groups i.e. BIPAR. The CEA interacts with many other groups at the EU level e.g. banking employers groups and trade unions. Indeed, the CEA attempts to become part of the process as early as possible and to this extent it has a good **relationship** with DGXV (ABI Representative).

When the proposal reaches the Committee of Permanent Representatives (COREPER) at the Council level, Permanent Representatives are urged to reach a **compromise** and ultimately a decision is **formulated.** There are varying accounts of the extent to which a sector/industry may be listened to at Council level. Consequently, it is important for the sector/industry to have the **support** of its Member State in respect of the legislation being **discussed.**

However, the further the **discussions** go in the Council process, the weaker the economic variables become.

A proposal is automatically despatched to Member State legislatures and relevant bodies, e.g. the DTI in the UK, and **opinions** on the proposal are sought. Interest groups also **lobby** at the national level. Consequently, legislation has **support** built into it through different avenues. The initiation of legislation is often a **"blurred"** (unclear in terms of **initiation**) activity. However, the industries/economic sectors are predominant in this initial area. When the proposal reaches the Council, **concessions** may have to be made to secure main points. The Third Life Assurance Directive was one where most difficulties seemed to be overcome in the initial stages. Germany pushed for more prescription but further **compromise** was reached (UK Permanent Representative).

It was accepted by the UK Permanent Representative that the move between the Member States trading situation and their **negotiating** positions indicate the changes the Member State wishes to bring about in its own regulatory environment. This allows the Member State to make changes without too much upheaval in respect of Member State legislation and regulation. It also provides the basis which the Member State uses when it approaches the **negotiating** process: it is **listening** to its sector/industry that has been **lobbying** at both the EU and national level. However, if it needs to ensure the legislation necessary it will **bargain** with its sector's/industry's wishes. This is once again indicated by the Council representative ". . . when it is considered that political variables take precedence at the Council level" (ibid).

The CEA does not only **represent** Member States but it does include the fifteen Member States (then twelve) in its membership of twenty three. It

deals mainly with national interest groups which are its membership. However, it will also **interact** with individual companies. Once the EU has created a **framework, discussions** will be undertaken in a number of **working groups** which are made up of national interest groups **representatives** and company **representatives**. Consequently, much **discussion** is undertaken in the pursuit of a **common understanding** between the Member States regarding the most **amenable legislation**. Of course, the Commission pursues the spirit of the treaty but also needs to know what is workable at the EU level. However, **conflict** between Member States creates **uncertainty** in what is necessary to enable the SEM: if separate Member State sectors all **lobby** the EU with **different ideas**, difficulties will arise. Basically, the European interest groups are central to the creation of the SEM because they create **agreement** and the consequent successful legislation. This illustrates the important role of European interest groups and the supranational bodies in the creation of the SEM.

Under the five main categories of **Understanding, Negotiation, Interaction, Difference** and **Compromise** a general comprehension of **European integration** is identified. The interview coding illustrates the parts individual institutions play in the formulation and construction of legislation. Primarily the five main coding categories are continually re-affirmed as the main processes of European integration. Indeed, this is further illustrated by the European Decision-Making Model below.

Survey B (see Appendix A p 291) was initiated to provide a general understanding of what UK Members of the European Parliament Finance Committee and lobbying groups considered to be the situation regarding life insurance regulatory environments. However, the response was low and shed minimal light on the situation. There was little difference in how the

UK political parties saw the situation. Each considered that the EU market in life insurance was liberal/prescribed and that was how it should remain.

Interest Group Membership in the UK

Finally, the model is further added to by survey C (see Appendix A). This survey asked the UK insurance companies the extent to which they used interest groups at the national and European level. Seventy questionnaires were despatched and twenty seven companies responded.

When the companies were asked if they used a European interest group in their participation in the formulation of the Third Life Assurance Directive, 81.4% said no, while 81.5% considered that they used a national interest group, in most cases the ABI and BIIC. The direct link between the European and national interest groups was further substantiated by questions three and four. 85.2% didn't directly use European interest groups at all, 74.0% contending that they didn't even subscribe to one. However, 100.0% of respondents subscribed to a national interest group (see appendix A). Even when their European interests were threatened, 77.7% of companies did not directly approach European institutions whereas 51.8% would approach their national government. However, 59.2% would usually use interest groups to lobby on their behalf at the European level and 89.9% at the national level. When asked if they prefer to use interest groups at the European level to enable the life insurance industry to make European-wide compromises, 81.5% of respondents rejected this idea. However, 85.2% used interest groups at the national level because this enabled nation-wide compromise. As the interviews have illustrated, it is then that the national interest group interacts with the EU and in the main it does this through European-wide

interest groups. In general, it is at this point that European-wide compromises are reached and the importance of European interest groups emphasised.

Of those respondents who indicated which interest groups they were members of, twenty were members of the ABI and two of BIIC; these two considered that through their membership of the BIIC they were affiliated to the CEA (the others did not say to which interest groups they were affiliated). However, none of the companies considered they were direct members of a European interest group. One respondent did point out that his/her company was a member of other national interest groups in other Member States that would seek to influence their views on important European matters.

The European Decision-Making Model

The European Decision-Making Model builds on Easton's (1965) model and illustrates how interests, preferences, motives and an overriding ideology transfer into demands in the national socio-economic environment and how a normative perspective of what is necessary is proposed at the European level by a particular Member State. This analysis investigates how such a proposal is subsequently presented at the EU level. One could list the above variables as requirements which are materialised within a definite ideological framework. Consequently, the model concentrates on the transfer of wants of a specific industry into demands at the domestic level and how these are then introduced to the political process at the European level.

One may consider that there are micro and macro elements to the model. The micro element concentrating on companies, national interest groups and national legislatures; and the macro aspect involved with European interest groups (or the meeting point of the national interest groups at the European

level) and EU decision-making institutions. The macro model would pick up on the micro model output and attempt to illustrate the process within a EU context. However, the two areas are interactive.

At the European level, there is an interaction between the subjective interests of the different Member State industries and the objective interests of the European institutions. This thesis considers that a compromise is reached at the European interest group level through the industries both interacting with one another and with the Commission and Parliament. The proposed legislation that goes through to the Council has been agreed by the Member State sectors/industries who either progressively or subsequently inform their own government of the situation in relation to the agreed legislation. During the process there may be disagreements between the Council and the other institutions.

Once the draft legislation is in the realms of the Council, certain agreements may be disposed of. However, one would expect the main tenets of the legislation to become law because the national sectors/industries would have compromised their positions at an earlier stage. Consequently, one would have expected them to lobby their government to accept the proposed legislation: the Council consists of representatives of the Member States. Indeed, it is the intergovernmental aspect of the EU decision-making institutions. If the draft legislation is extensively interfered with by the Council, under the Co-decision procedure, the European Parliament may intervene.

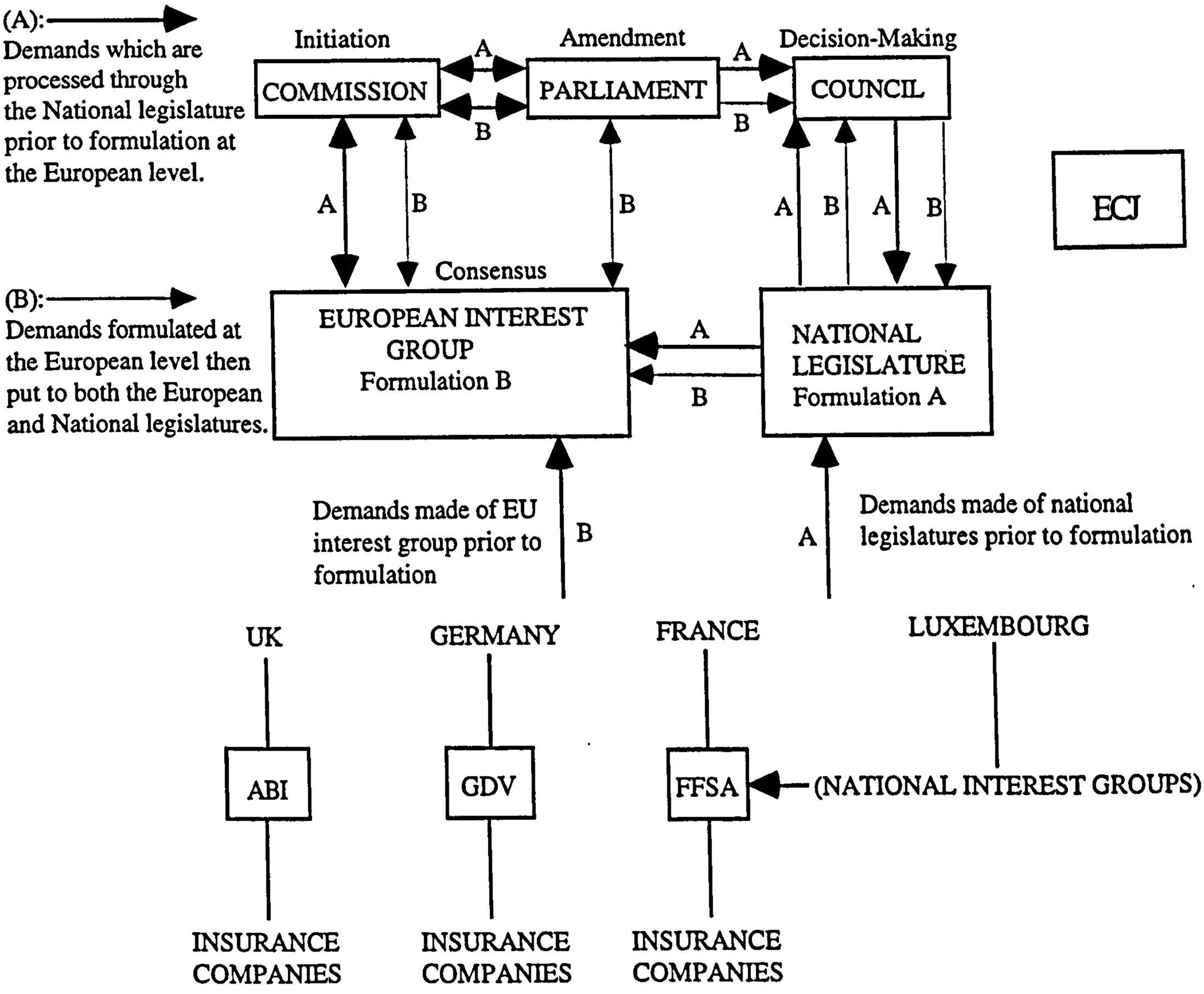
The interviews indicated agreement on a number of points: the Third Life Assurance Directive was unanimously perceived as a means of providing the environment that would allow mutual recognition to be achieved; it was also

acknowledged that many influences went into the drafting of a directive. Since 1988, interaction between industries and the Commission has become more apparent at the EU level. The representative of DG XV considered that ongoing contact with the life insurance industry was imperative in respect of legislative input. Most importantly, the interviews illustrate the interactory procedures at work in the formulation of the Third Life Assurance Directive and the extent of the use of interest groups in the process. However, what is also clear is the intergovernmental aspects. The following understanding of the process and decision-making model (see Fig 7.3 p 243) was accrued from the interviews and survey C.

For the purpose of this study, the European Court of Justice (ECJ) is not discussed. There are a number of issues that need to be explained with regard to the model. Firstly, the survey regarding Member State interest group membership and the interviews illustrated that the majority of life insurance companies were members of national interest groups. Further interviews indicated that national interest groups were affiliated to interest groups at the EU level (mainly the CEA and BIPAR). Secondly, in the formulation of legislation (although Member State interest groups may approach the European institutions), the Commission and European Parliament preferred to deal with European-wide interest groups because these allow a European picture of the situation. Thirdly, because the sector understands what is necessary for the successful operation of the embryonic regulatory environment, it is highly likely that they will confer and reach some agreement prior to national, i.e. Council or intergovernmental interference.

FIG 7.3

THE EUROPEAN DECISION-MAKING MODEL



Finally, the interviews with the CEA, the ABI, the BIIC and members of EU decision-making institutions substantiated that other Member State insurance industries actively participated in the creation of EU legislation through interest groups.

There are two general directions that could be taken regarding decision-making procedures identified on the model shown in Fig 7.3. These are indicated by arrows A and B; process A considers that demands are formulated through the national legislature prior to formulation at the EU

level, whereas route B illustrates demand formulation being compromised at the EU level prior to the involvement of the national legislature. Route A is a stronger intergovernmental approach whereas route B illustrates more of a neo-functional process. Of course, the situation is not as straight forward as the model outlines. Indeed, elements of both routes were in use, but in general the interviews emphasised route B (see Fig 7.3).

The European interest group rarely had any dealings with the national legislature and interaction between the two was undertaken between the national interest group and the national governmental departments (the DTI in the UK). Consequently, at this point there is intergovernmental involvement even though it is minimal and in most cases the DTI adheres to decisions already made at the EU interest group level. More importantly, there is intergovernmental involvement apparent in the Council. However, since the SEA and QMV, this has been minimised because if a directive is to be successful it needs only the support of a qualified majority of Member States, not all of them.

The interviews illustrate that agreement is sought at the European interest group level and through negotiations with the Commission and Parliament usually established. Indeed, if legislation is being negotiated by the industry through interest group involvement with a supranational institution (EU decision-makers) the research has uncovered elements of neo-functionalism. If a compromise is not reached at the EU level, then each Member State industry would pursue its own ideal market type (as indicated by the matrices see figs 5.1 and 5.2) and compromise would be difficult if not impossible to achieve. To enable successful acceptable legislation at the EU level, the interviews and surveys illustrate that both neo-functional and intergovernmental processes need to be at work. Indeed, even if a total neo-

functional process is not at work, it is at least a form of multi-level governance.

Conclusion

This thesis considers that the interviews identify a process that is formalised through the models. Easton's Demand model illustrates the process in abstract terms (see Fig 7.1). This is transferred into a European Demand Model (see Fig 7.2) Indeed, this illustrates the six aspects of wants becoming demands on the European Union and national legislatures. Finally, through the use of the European Demand Model, Easton's adapted Demand Model and the interviews, an EU Decision-Making Model is formulated (see Fig 7.3).

The Commission initiates legislation at the EU level. Indeed, ". . . the Commission is a critical actor in the policy initiation phase . . . After surveying the evidence one cannot conclude that the Commission serves merely as an agent of state executives" (Hooghe and Marks, 1997; p 28). Indeed, ". . . if supranational policy-making institutions emerge there is an inherent 'logic' of interest group interest group behaviour which will lead interest groups to re-target their lobbying strategies to take account of the new distribution of power. . . . If power has shifted to a new level of government, any sensible interest group is bound to attempt to influence at the new level. As one American interest group official put it, you need to shoot where the ducks are!" (Mazey and Richardson, 1996; p 200).

The empirical work identified that interest groups were central to the decision-making process. Indeed, in relation to the Decision-Making Model the route provided by the B arrows is the one best supported by the interviews. Compromises are initially formulated at the national level which

are then relayed to the European interest group. Through interaction and compromise a European perspective is sought and eventually put to the national and European decision-making institutions. Of course, there is also input from the national and EU legislatures while this European-wide stance is being formulated. Effectively, an all-round compromise is created which should enable successful legislation. Theoretically, once the Council level is reached, there should be general acceptance of the proposed legislation.

In general, the industry/sector creates an **understanding** of the preferred regulatory environment at the national interest group level: this **understanding** is consequently **negotiated** and **compromised** at the European interest group level. Through **interaction** with the Commission and Parliament, the institutions and the European interest groups come to an **understanding** on legislation that is acceptable to the majority of Member States. In some instances national interest groups and individual companies will attempt to **interact** with the Commission. However, the Commission does make it clear that it prefers to **negotiate** with European interest groups because this enables a European-wide perspective. This was made clear by all of those interviewed. Once the legislation has been agreed at this level it needs to go through the European legislative process. When the proposals reach the Council level, **difference** should have been minimised either because the Member State interest groups or the European interest groups would have informed governments of the industry's/sector's general acceptance of the directive. If there is no general **agreement** the directive will either fail or remain on the table. There are exceptions to this process and certain parts of proposed legislation may be discarded. However, in a post-SEA and SEM Europe there has to be a general means of reaching a **compromise** in terms of effective legislation.

The thesis considers that a means of reaching a **compromise** is illustrated here and that in the above context elements of a neo-functional process are observable. The work illustrates a supranational body toward which national organisations have partially shifted their allegiance. If European interest groups and supranationality are employed in the creation of legislation then neo-functionalism as well as intergovernmentalism is apparent in the integration process. Indeed, if the above is considered to be the norm in a post-SEA EU, then one may posit that this process will also involve spillover in the financial services sector. The following chapter explores such a scenario.

Chapter Eight

European Financial Services Legislation: A Case of Spillover?

> *It is obvious that no matter how complete the theory may be, a middle term is required between theory and practice providing a link and a transition from one to the other. For a concept of the understanding, which contains the general rule, must be supplemented by an act or judgement whereby the practitioner distinguishes instances where the rule applies and where it does not (Kant, 1995; p 61).*

Introduction

This chapter examines the amount of legislation currently in operation and the amount that is necessary to create a single market in financial services and capital movements. The thesis accepts the above understanding of the EU decision-making process and posits that through this a spillover process is identifiable in the EU with regard to insurance and financial services legislation. It generalises the processes identified through the interviews and considers extending the model and its theoretical implications. Indeed, a qualitative analysis extrapolates from one specific situation to another similar situation, rather than from a sample of a population to the total population. Consequently, this thesis posits that, the process taking place with regard to life insurance is likely to be happening from industry to industry and from sector to sector. The thesis does recognise the limitations of such a generalisation and does so with these in mind. Indeed, industries and sectors

are on the one hand isolated entities concerned with their own situation in the wider market place. However it is through this self interest that they must be aware of what is happening in other industries and sectors. This in turn makes them initiators of and reactors to the actions of other industries and sectors. Consequently, there exists a process of spillover.

> Neo-functionalists such as Haas, purport to describe the mechanism of the linkage between integration in economic and political sectors through the concept of spillover. They use the concept to describe a dynamic and more or less automatic integrative process, gradually encompassing ever more functional sectors until, the final stage, a political union is reached (Kirchner, 1976; p 2).

The objective of this chapter is to identify the links between the legislation in financial services, discuss the concept of spillover and the implications this has for European integration.

> The current ascendancy of a qualified supranational style of decision-making is shown by the way in which, thanks to the Single Act, the Council now functions. . . . The revival of a supranational style of decision-making and the strengthening of European institutions in the Single Act resulted most immediately from decisions by governments to press in their own interests, for a removal of internal economic barriers and for institutional change that would permit such a policy to be carried out (Keohane and Hoffman, 1991; pp 16-17)[1].

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[1] At the time of writing, an impasse was apparent regarding pensions, taxation and capital markets, because they come under the unanimity rule. However, these one may assume, will have to be overcome either just before or, more likely, following monetary union.

Indeed, the thesis considers that spillover may be divided into two areas: intergovernmental and neo-functional. Intergovernmental spillover provides the Treaties and decisions made at intergovernmental conferences, e.g. the creation of the ECSC and the shift to the EEC. Neo-functional spillover can be broken down into three areas: vertical spillover (within the same industry); horizontal specific spillover (within the same sector); and horizontal general spillover (sector to sector). Through an interaction between intergovernmental and neo-functional spillover integration is intensified (for an illustration of this see the Spillover Model, Figs 8.1, 8.2 and 8.3 pp 277-81). Consequently, the thesis recognises that intergovernmental processes are at work within the creation of the single market, i.e. in the guise of the SEA and the Maastricht Treaty. Fundamentally, it is considered that ". . . spillover requires prior programmatic agreement among governments, expressed in an intergovernmental bargain. Such a bargain is clearly important in accounting for the Single European Act" (Keohane and Hoffman, 1991; p 17). However, it is also thought that neo-functional processes are also providing an impetus to harmonisation and integration. In this context, the thesis contends that intergovernmental spillover provides the environment for neo-functional spillover to take place i.e. through the ECSC, the EEC, the SEA and the Maastricht Treaty. However, it also considers that the Member States are pushed in this direction by the dynamics of neo-functional spillover. Indeed, as it becomes more difficult to pass further directives/regulations in an area, further amendments to the Treaties are needed. This was apparent with regard to the SEA and the Maastricht Treaty and may become even more explicit with the Treaty of Amsterdam and the actuality of monetary union. The accumulation of legislation towards monetary union, which in itself overcomes a number of difficulties (as an element of intergovernmental spillover) adds impetus to further

harmonisation. Finally, this chapter overviews elements of intergovernmental and neo-functional spillover in respect of: the Cecchini Report, the White Paper (1985), freedom of establishment and services, harmonisation, mutual recognition, the SEA, the SEM, the Maastricht Treaty, EMU, and relevant European Court judgements[2].

Financial Services and Intergovernmental Spillover

The Cecchini Report was put forward as a rational argument for the provision of an actual SEM. Indeed, following the White Paper, the report illustrated the need for the SEA if the impasse that European integration had reached was to be overcome. If a common market was to be realised then further intergovernmental spillover was necessary. Cecchini proposed that national standards and regulations were what European businesses perceived as the second most important NTB to be removed (Cecchini, 1988; p 5). The importance of the service sector was not under-estimated in the report, although the extent to which the figures may now be relied upon are debatable. The thesis does not wish to give a prognosis on the validity of Cecchini's calculations. It does, however, wish to draw on certain qualitative conclusions that the report displayed.

Cecchini contends that the role of the service sector in Europe is one of ". . . growing importance . . ." and that ". . . the potential for much more significant growth is being artificially pinned back by regulations which

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[2] There have been two major judgements regarding financial services. The first was made in 1979 in the Cassis de Dijon case which allowed *mutual recognition* (see below). The second was made in 1986 in response to four Member States (Denmark, Eire, France and Germany) that were imposing Non-Tariff Barriers (NTBs) to prevent insurance companies in other Member States from entering their markets. The judgement in the second case considered that the NTBs were partially illegal but partially justified. The judges felt that they were justified with regard to consumer protection which in the field of insurance is particularly important. However, the judges excluded from this all those risks for which such protection was not necessary i.e. large scale risks whose expertise would not necessitate special consumer protection. The benefits of this judgement were included in the insurance directives of the following years.

significantly inhibit the free flow of services and thus the free play of competition between companies . . ." (ibid, p 37). Cechinni spoke of the pivotal role that financial services would have in the creation of the single market.

> Basing its figures on a survey conducted on the three main areas of financial services activity . . . the report forecasts gains of ECU 22,000 million for the eight Community countries Belgium, France, Germany, Italy, Luxembourg, Netherlands, Spain and the UK . . . the value-added generated by the credit and insurance sectors alone accounted for some 6.5% of the Community's gross domestic product in 1985. . . . The benefits would be even greater if the freedom to provide within a European financial common market could be linked immediately to a common currency, since exchange costs would disappear and businesses and individual consumers could achieve substantial savings (European Document, 4/1989; p 7).

Additionally, the freedom to provide cross-border financial services in tandem with liberalised capital movements would create a more attractive environment for financial business and produce a better means of channelling savings into investment projects. The difficulties created by national capital markets in the EU were highlighted in a Commission report dated April 1983. It contended that even though gross savings in the EU amounted to ECU 430,000 million and in the USA, ECU 340,000 million, the amount mobilised for investment in the EU five leading markets (France, Germany, Italy, the Netherlands and the UK) was less than in the USA (ECU 212,000 million in the USA, ECU 142,000 million in the EU). This illustrated the difficulty of mobilising capital in smaller national financial markets (ibid).

"Financial services such as banking and insurance will be among those to benefit most from the removal of all barriers and the completion of a large internal market" (ibid, p 18).

By the early 1980s it had become clear that the EEC was far from a common market: fundamentally it was an uncommon market[3]. Indeed, NTBs were ensuring that a true common market could not develop. In 1985, the Commission put forward plans to remove physical, technical and fiscal barriers between Member States by 1992. "Financial services . . . including insurance, were to be governed by three major principles, i.e. minimum co-ordination of individual national rules, mutual recognition and home country control" (ibid). This indicated the need for Treaty amendments and these were encapsulated in the SEA.

The SEA necessitated a number of amendments concerning the free movement of services and capital that are displayed in Articles 52-73 of the amended Treaty. These illustrate intergovernmental spillover and are the basis from which further neo-functional spillover could take place:

(1) Right of Establishment (Arts 52-58).

(2) Services (Arts 59-66).

(3) Capital (Arts 67-73).

The programme of a SEM is a continuous process of change that is built on the basic tenets of the (Treaty of Rome, 1988; Arts 2 and 3) and one that will

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[3] This term is taken from Stuart Holland (1980) who considered that in 1980 the void between theory and practice regarding the EU was immense: that the Common Market was not such at all but an uncommon market in terms of national self-interest. Effectively, it encapsulated no more than a Custom Union. Additionally, the idealism of integration has been misplaced in that ". . . the Community is essentially a capitalist market, uncommon and unequal" (Holland 1980 p 8).

evolve as further treaties come into effect. This process of change had already begun and has carried on in a post-SEM Europe.

Freedom to Provide Services and Freedom of Establishment

The freedom of services and the freedom of establishment are material illustrations of the ways that the Treaty provides the environment for neo-functional spillover. The Treaty contends that the freedom to provide services and enable the freedom of establishment should have been realised by 1969.

> The Treaty states that freedom of establishment encompasses the taking up and carrying out of own-account gainful activities such as the founding of undertakings . . . (and) that the freedom of banks and insurance companies to provide the services be established in step with the gradual liberalisation of capital movements (European Documentation, 4/1989; p 7 author's brackets)[4]

The difference between freedom of services and freedom of establishment may be illustrated in the following terms. Freedom of services is a temporary and occasional expansion of an activity normally carried out within the principal place that the business is situated in (the territory of another Member State). The freedom of services concludes and establishment begins when, in the course of business, the foreign insurer uses the services of an

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[4] There is also some debate as to whether insurance services actually come under Article 59. To decide this, it is necessary to ascertain where the insurers perform their services; if business is performed in their principal place of business then there is no freedom of services. If business is performed where the risk is incurred or where the activity takes place, then the service should be judged by Article 60 (1); this is where activities are carried out in another Member State for the purpose of performing the service. In the case of insurance, this is where insurance activities are carried on for the purpose of taking out or implementing insurance policies.

agency or an authorised representative within the Member State. With regard to this difficulty, the ECJ made the following point:

> In this respect it has to be admitted that an insurance enterprise of another Member State that maintains a constant presence in the Member State concerned is subject to the provisions of the Treaty on the right of establishment. . . . In view of the definition in Art 60 (1) of the EEC Treaty referred to, therefore, such an insurance enterprise cannot rely on Arts 59 and 60 of the EEC Treaty with regard to its activities in the Member State concerned (cited in Parliament Working paper, 1992; p 8)[5].

With the basis in place, there is a need for further clarification and in some cases more legislation. The problems concerning different types of regulation become more precise and these are dealt with through: harmonisation; mutual recognition; and home country control.

Neo-Functional Spillover, Mutual Recognition and Home Country Control

One may consider that one person's protective legislation is another person's trade barrier (see Chapter Five) and it is from such a premise that the EU undertakes a harmonisation process under a tripartite system:

- the harmonisation of essential standards.

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5 Consequently, services with regard to life insurance are: (a) Performed by insurance enterprises that are licensed institutions with their principal place of business in a Member State; (b) For a policy-holder or insured person that is resident in another Member State; (c) For the purpose of taking out, administering or implementing insurance policies; (d) Not included under the rules of establishment. Article 52 (ibid). .Basically, in the area of life insurance the liberalisation Article 59 (1) is subject to the provisions of Article 61 paragraph (2).

- the mutual recognition of other Member State standards

- (based on the above) home country control and supervision.

The liberalisation of insurance, banking and security markets is tied closely to the free movements of capital and the Treaties contend that the liberalisation of the banking and insurance sectors ". . . shall be effected in step with the progressive liberalisation of the movement of capital" (HMSO, 1988; Art 61). Thus, through intergovernmental spillover there is an opportunity for general horizontal neo-functional spillover (sector to sector or services to capital) and horizontal specific neo-functional spillover (industry to industry or banking to insurance) and vertical spillover (within the same industry i.e. insurance) is created. This is a good example of intergovernmental spillover providing the initial impetus (see the Spillover Model, Figs 8.1, 8.2 and 8.3 pp 277-81)[6] .

The Treaties indicated that the EU should be attempting to create a functioning SEM. However, it may be argued that intervention in legislative processes should be limited to the domains in which mutual recognition cannot ensure the protection of essential requirements. To assist in the convergence of legislation, the EU could take measures to promote the transparency of transposing legislation at the national level through exchanges of information and allowing the national courts a greater capacity for ensuring the adherence to EU legislation.

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6 As argued above, there are two processes of spillover at work: one at a national level and one at a supranational, sector and interest group level. The former may be identified as intergovernmentalism, the latter as neo-functionalism. The latter may be broken down into three areas: general horizontal spillover (services to capital, etc); specific horizontal spillover (insurance to banking, i.e sector bound); and vertical spillover (within insurance) The Spillover Model identifies legislation that has incrementally been formulated since the inception of the EEC. The model identifies the legislation with a cross and number and these correlate with the itemisation included in the model below. Indeed, neofunctional spillover is identified through this itemisation whereas intergovernmental spillover is indicated on the left hand side of the model through landmarks such as the SEA, Maastricht and EMU.

A legislative framework should respond to the objectives of free movement and the respect of essential requirements immediately. However, at the same time, it must also adhere to the objectives of a balanced social and economic development.

To enable the achievement of an SEM, the Commission concluded that the regulatory framework may be achieved through mutual recognition and home country control. The 1985 White Paper proposed that the minimum of essential standards should be harmonised. The difficulty is how to interpret 'essential' and 'minimum' in respect of the proposed regulatory framework. As illustrated in Chapter Five, each Member State will have a different interpretation of these terms which will be reflected in its existing legislation and consequent regulatory environment. The thesis has proposed that norms of a legal nature must differ from state to state; consequently, a process of compromise may be discerned through the construction of the legal framework that will indicate both the future and present state of the SEM regulatory structure (see Figures 5.1 and 5.2 pp 157 and 160). Indeed, chapters Five, Six and Seven concluded that national legislation is compromised by Member States through the use of interest groups and supranational authorities (see the Decision-Making Model, Fig 7.3 p 243). Mutual recognition encapsulates an important mechanism in the pursuit of the SEM as it gives a framework for compromise. However, as the thesis has indicated (see Chapter Five) where diversity is so great, there will be a need for greater rather than less harmonisation of Member State legislation.

> The principle of mutual recognition . . . pre-supposes agreement on a number of basic rules . . . these minimum harmonisation requirements . . . are only possible because common interest,

> mutual confidence and a high degree of economic convergence exist between EEC member states (Loheac, 1991; p 409).

One has to question if "minimum harmonisation requirements" have been met in respect of the life insurance market. The achievement of such requirements is extremely rare and even if there is a ". . . high degree of economic convergence" in the life insurance market, the practical realities of achieving an SEM through mutual recognition alone are apparent (ibid). A convergence process must be undertaken prior to the actions of mutual recognition coming into play (see Figs 5.1 and 5.2).

The idea behind mutual recognition suggests spontaneous legislative adaptation. However, it does not deal with all regulation and as a convergence point is necessary for mutual recognition to be effective it could be conceived as an impetus that encourages legislative change and compromise.

Following intergovernmental spillover, the convergence process illustrates neo-functionalism because agreement between Member State industries has to be reached, as does agreement between the Commission and the industry in general. This allows the formulation of legislation that is agreeable to both the Member State industries and the EU and increases the chance that the legislation will be successful at the Council of Ministers' stage. Directives allow Member States to build legislation into their own legal frameworks and to allow this, they are quite broad in character. At this point, mutual recognition comes into play and the theory is that this will allow convergence through market forces. However, mutual recognition usually requires prior compromise and convergence. This thesis considers, that it is such a process as this that indicates neo-functional spillover in the creation of the legislation

that underpins regulatory structures. Indeed, the processes of legislation creation encompass the nuts and bolts of European integration.

European Banking Legislation

The banking sector has been affected by two co-ordination directives. The First Banking Directive (77/780/EEC)[7] cleared most obstacles to the freedom of establishment for banks and other credit institutions, introduced home country supervision and a common position for the granting of banking licences. However, problems were still apparent and certain obstacles needed to be removed before a genuine single market in banking could be achieved.

The Second Banking Directive (89/646/EEC)[8] aimed at the removal of authorisation problems i.e. 12 different supervisors, a definition of banking activities and cross-border trade. Consequently, the second directive enabled a single banking licence, a list of banking activities and minimum capital levels (5m ECU laid down for new banks). The directive also provided supervisory rules in terms of internal management, audit systems and the amount of control of major shareholders.

The Directive on Investment Firms and Credit Institutions (CAD) provides the framework for the Investment Services Directive (ISD) (93/22/EEC)[9]. The two directives engender an internal market in respect of investment services and give all institutions, whether credit or investment firms, the ability to offer investment services throughout the EU. This illustrates general horizontal neo-functional spillover (sector to sector or services to capital). In this context, the sectors are intrinsically linked.

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7 OJ L 322 17/12/77
8 OJ L 386 30/12/89
9 OJ L 141 11/06/93

In December 1992, the Council adopted the Directive on Monitoring and Controlling Large Exposures of Credit Institutions[10]. As part of the legislation necessary to create an SEM in the banking sector, it deals with the prudential treatment of large exposures with a single client. Large exposures are defined in the Own Funds Directive (89/299/EEC)[11] in which an exposure is considered large if it exceeds 10% of the credit institution's own funds. The Directive states that companies should make known the existence of all large exposures and none should exceed 25% of the credit institution's own funds.

At the ECO/FIN Council on 23 Nov 1992, the Commission's approach to the BCCI affair was outlined by Sir Leon Brittan. He contended that the system of home country control and consolidated supervision did not need major reforms. However, he contended that in certain respects supervision may be strengthened and clarified, particularly with reference to: the transparency of group structures; greater exchange of information between supervisory authorities; the role of external auditors; and intensified co-operation between international prudential supervisors. The 35th meeting of the Banking Advisory Commission was consulted in respect of the draft proposals of the Commission. This concerned a directive to amend the Council directive on strengthening the supervision of credit institutions following the discussions on BCCI at the ECO/FIN meeting. The Banking Advisory Committee also discussed a broad outline by the Commission on amending the Council Directive concerned with the re-organisation and winding-up of credit institutions.

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[10] OJ L 29 05/02/93
[11] OJ L 124 05/05/89

In general, during the nineties, there have been numerous decisions made by the Commission and Council as well as further directives with regard to the banking sector. For instance, Council Directive (96/13/EC)[12] amends article 2 (2) of (77/780/EEC)[13] in respect of the list of permanent exclusions of certain credit institutions. Indeed, directive (96/10/EC)[14] amends directive (89/647/EEC)[15] regarding contractual netting by competent authorities; directive (95/15/EC)[16] and (94/7/EC)[17] amend the directive regarding solvency ratios. Effectively, the last directive in terms of banking that was not an amendment to a previous directive was (93/6/EC)[18] which covered both investment firms and credit institutions and subsequently both security markets and insurance as well. Fundamentally, banking legislation and its consequent regulation spills over and necessitates legislation in other financial services industries. This process is illustrated by the interaction between security markets and banking. Indeed, one may consider that this is an example of neo-functional horizontal specific spillover; or spillover within the same sector.

European Security Market Legislation

The objective of an SEM in security markets is one in which companies are free to raise capital and be admitted to stock exchange trading in other Member States, as easily as they may in their own. The directive (80/390/EEC)[19] was the first step in the process and it indicated the harmonisation of conditions for stock exchange listings and agreed mutual recognition in respect of any listing that met 1980s particulars. In 1993, a

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12 OJ L 066 16/03/96
13 OJ L 322 17/12/77
14 OJ L 085 03/04/96
15 OJ L 125 05/05/89
16 OJ L 125 08/06/95
17 OJ L 089 06/04/94
18 OJ L 141 11/06/93
19 OJ L 100 17/04/80

proposal to amend this Directive was posted[20]. The aims of the proposal were to simplify cross-border listing requirements for established companies and to facilitate the listing of companies on junior markets. The amendments are an extension of Article 6 and are based on the assumption that most of the information needed by investors already exists in the market. Therefore, its duplication to ensure consumer protection is no longer justified.

The proposed amendments of (80/390/EEC) should engender more efficiency in the securities market as the proposed legislation is more beneficial to the realities of the existing market; the measures relating to cross-border listing would also assist the implementation and completion of the EUROLIST project which is to be launched by the Federation of Stock Exchanges at some point in the future.

Directive (85/611/EEC) on undertakings for collective investment in transferable securities (UCITS)[21] from October 1990 allowed an investment fund authorised in its home Member State to be sold anywhere in the EU. An amended proposal for a Council directive was adopted by the Commission in December 1989[22]. This complemented the Second Banking Directive and provides for the liberalisation of security-related services provided by non-banking intermediaries. It introduced cross-border provisions in respect of broking, dealing and portfolio management. The directive also allows anyone authorised by their home country to be a member of their national stock exchange to be a member of any other Member State stock exchange. This is a major difficulty as there should be no dictate on how a Member State should run its own stock exchange. Discussions with Member States are at an early stage and progress is very slow. One may consider that this is because further

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20 OJ C 23 27/01/93
21 OJ L 1995 375/3
22 Com (89) 629 final-SYN 176

changes are necessary and these can only be realised through monetary union (intergovernmental spillover through the Treaty of Maastricht).

European Insurance Legislation

Insurance legislation is an example of vertical neo-functional spillover or spillover within the same industry. Initially, there were two general programmes proposed to ensure that both the freedom of services and establishment would be realised in life insurance by the beginning of 1970. This was indicated through five main bi-annual target dates.

1964 Reinsurance. Freedom of establishment and services.

1966 Indemnity insurance. Freedom of establishment.

1968 Life insurance. Freedom of establishment.

1968 Indemnity insurance. Freedom of services.

1970 Life insurance. Freedom of services.

As may be observed, life insurance was to be harmonised in two stages which would have corresponded with the initial plans for Monetary Union. However, decision-making was difficult and the timetable too crowded. The programme was an over-ambitious attempt to align substantive law. During the 1970s, this was replaced with equivalence and mutual trust between Member States and the harmonisation of substantive law kept to a minimum.

EU legislation has primarily taken a three dimensional approach to insurance. Following Council directive (64/225/EEC)[23] that abolished restrictions on freedom of establishment and freedom to provide services

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[23] OJ L 56, 04.04 1964; p 878

concerning reinsurance and retrocession, insurance has been broken down into non-life and life. Reinsurance was the easiest to harmonise because it was international by nature. Consequently, the harmonisation of national legislation was less of a problem. The life and non-life areas of insurance have had to deal with differing national regulations conceptualised in historical normative ideas of what constitutes insurance products, consumer protection and choice. These problems have affected non-life insurance. However, the most difficult problems to be overcome have been those that pertain to the life insurance market.

In its proposal for a the Third Life Assurance Directive, the Commission emphasised that ". . . the internal market in insurance represents a primary goal . . . in view of the importance of this strongly expanding sector"[24]. The insurance industry considered that it needed priority treatment because it lagged behind the liberalisation of the other economic sectors within the financial services sector (omitting pensions). Directives in the securities and banking industry had already been implemented and as a consequence the insurance industry had been left at a competitive disadvantage in relation to these industries. Indeed, an example of horizontal specific neo-functional spillover (within the same sector) and with regard to Capital legislation, horizontal general neo-functional spillover (from sector to sector).

In terms of vertical neo-functional spillover, the adopted insurance directives have taken form in three generations dating from the early 1970s: these are briefly overviewed below. Directives concentrating on more specific areas include the Council directive on measures to facilitate the effective exercise of freedom of establishment and freedom to provide services in respect of the activities of insurance agents and brokers (ex ISIC group 630) and in

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[24] Com 91 57 final SYN 329 p 2

particular, transitional measures in respect of those activities (77/92/EEC)[25]. The Co-Insurance Directive (78/473/EEC)[26], the Credit and Suretyship Assurance Directive amending Directive (87/343/EEC)[27], and the Legal Expenses Directive (87/344/EEC)[28]. The latest, more specific, directives include the Council Directive on the Annual Accounts and Consolidated Accounts of Insurance Undertakings (91/674/EEC)[29] and the Council Directive setting up an Insurance Committee (91/675/EEC)[30]. The former of these Directives proposes the harmonisation of EU insurance accounting practices which is necessary if valuation and solvency indicators are to be uniform. The latter directive provided a committee to act as an intermediary between the industry and the Commission and to assist in implementation procedures. The committee also examines any questions relating to the application of existing directives and the preparation of new legislation proposals in the insurance sector. The Insurance Committee met in Brussels on 24-25 May 1993 where the most important items on the agenda consisted of consultation for a Directive which would take into account the BCCI experience; the problem of Member State legislation implementation; the proposal for an EC Co-operative Company and its effects on insurance supervision. All of this legislation is not depicted on the spillover model because this would make it unclear. However, elements could be included as each has an influence on the other and provides an illustration of neo-functional spillover (see the Spillover Model, Figs 8.1, 8.2 and 8.3).

Also under discussion during the early nineties was the proposal for a Council directive on the co-ordination of national laws, regulations and

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25 OJ L 26 31/06/77
26 OJ L 151 07/06/84
27 OJ L 185 04/07/87
28 OJ L 185 04/07/87
29 OJ L 374 31/12/91
30 OJ L 374 31/12/91

administrative provisions relating to insurance contracts[31]. This was discontinued in 1993. As discussed above protection against divergent contracts may be used as an NTB because unfair contract protection is different in the different Member States. However, the implementation of the EC Unfair Contract Terms directive in 1993 has reduced the extent to which insurance contracts can be used as NTBs. Indeed, ". . . by converting common law self regulatory Statements of Insurance Practice into statutory codes applying to all insurance companies trading in consumer risks within the UK market" (Ellis, 1995; p 54). According to Ellis this could be seen as "inward" spillover. One where a general piece of European legislation overcomes difficulties in specific sectors. Indeed, even though this does not completely deal with the difficulties that emerge from the lack of an insurance contracts directive. It does, however, allow a benchmark for contract terms that may be acceptable in the European Union. This illustrates spillover and provides a starting point for harmonisation in the European life insurance industry. Still under discussion is the proposal for a Council directive on the co-ordination of the laws, regulations and administrative provisions relating to the compulsory winding up of direct insurance undertakings[32].

Each of these proposals relate to consumer protection, while at the same time they attempt to ensure consumer choice and a competitive market. However, Member States have difficulty in reaching a compromise with the EU in these areas because of both sovereignty and regulatory environment issues. These directives are more generally known as the Contracts and Liquidation Directives. The first Council discussion on the contracts proposal was in 1980[33] with the latest taking place in 1988[34]. Council discussions on the

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31 OJ C 71 28/07/79
32 OJ C 71 19/03/87
33 OJ C 355 31/12/80
34 OJ C 235 06/10/89

liquidation amendment began in the first six months of 1993. The problems in these areas reflect those experienced by the third generation life and non-life directives.

Finally, in respect of further spillover, it is worth noting the overlap with regard to the legislation between these three areas: much of it will lay the basis for future legislation in areas not sufficiently touched upon, i.e. pensions and taxation. Financial services legislation has created difficulties for other sectors which has necessitated further legislation. This is general horizontal spillover as there is a task expansion from one sector to another, e.g. from services to capital. However, there is also spillover from one area of financial services to another, e.g. from banking to insurance, and this is specific horizontal spillover. Additionally there is vertical spillover and this is illustrated by legislation in one area of the sector, e.g. insurance, creating the necessity for further legislation in the same area (see below). The non-life insurance directives are, on the one hand, tied closely to the life insurance directives, while on the other, like their life insurance counterparts, they border banking and security services legislation. Effectively, there has been a task expansion throughout the sector and one may consider that this encompasses a form of spillover.

The Life Assurance Directives

As mentioned above, the life assurance directives illustrate specific neo-functional spillover (this is spillovers most simplistic form) with each generation creating the need for the next. However, each generation also created the need for further legislation, both in insurance and other areas of financial services. The first generation of directives allowed for the freedom of establishment as long as conditions of contracts and tariffs were

approved by the Member State in which the company wished to establish. The First Life Assurance Directive dealt with the need for licensing and the means by which an insurance establishment would be approved and standardised. Additionally, the supervisory responsibility in respect of establishment competence was transferred to the Member State where the principal place of business was situated. However, there was little legislation regarding freedom of services in this directive.

The Second Life Assurance Directive (90/619/EEC)[35] provided the means for cross-border business and delineated the active and passive provisions of services. The directive takes the consumer as its starting point and provides for free movement through two regulations. Firstly, if policy-holders approach an insurer from another Member State, the legislation of the Member State where the insurer has its majority of business applies. However, secondly, if the insurer attempts to persuade the policy-holder to take out a policy, the legislative code of the Member State in which the insurer performs a service applies. This denied cross-border trade in life insurance and necessitated further harmonisation. This led to the Third Life Assurance Directive and a process of specific vertical spillover.

The Third Life Assurance Directive (92/96/EEC)[36] was adopted on 10 November 1992 and implemented on 1 July 1994. Fundamentally, it creates a uniform system of control in that insurers need only to be granted approval where they have their headquarters and control should be administered by their own Member State. It amends both former directives and specifically removes the passive/active clause from the Second Life Assurance Directive (see Appendix C, Article 4 the Third Life Assurance Directive). In general

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35 OJ L 330 29/11/90
36 OJ L 360 09/12/92

terms, host Member State legislation only applies if it is considered to be for the general good - this incorporates the permitted application of host country rules where there is no duplication in the country. The general good should also be applied without national discrimination and proportionate to the objective being pursued.

The main provisions are as follows. Firstly, there is the single licence, this shifts responsibility for financial supervision (in terms of all business) to home country or head office supervision. This is whether policies are written through:

(a) a head office; or

(b) a branch in another Member State; or

(c) a service basis.

There is no need to seek authorisation. The undertaking should simply notify the authorities (see Appendix C, Articles 3 and 4 the Third Life Assurance Directive).

Secondly, the directive pursues uniformity in terms the assets to be used to represent the solvency margin in respect of:

(a) accounts of Mutuals;

(b) preferential share capital;

(c) subordinated loan capital; and

(e) undated securities (see Appendix C, Article 8 the Third Life Assurance Directive).

Thirdly, the directive indicates actuarial principles governing the calculation of technical provisions. It also requires premiums for new business, on reasonable actuarial assumptions, to enable insurers to establish adequate

technical provisions (see Appendix C, Article 17 the Third Life Assurance Directive).

Fourthly, regulations on matching and localising assets representing the technical provisions are provided. This is done with regard to:

(a) the currency matching of the asset representing the technical provision;

(b) the extent that assets must be both adequately spread and diversified;

(c) how far and which assets may be used to represent technical provisions;

(d) the limitations of certain assets.

It is also stated that Member States are not allowed to determine insurers investment categories (see Appendix C, Articles 20 and 21 the Third Life Assurance Directive).

Additionally, the directive deals with qualifying holdings, composite insurers, contract cancellations and disclosure. Qualifying holdings are demarcated as 10%-plus of capital or voting rights; or that which enables significant influence over the management of the given undertaking (see Appendix C, Article 14 the Third Life Assurance Directive). The competent authorities need to be notified about existing qualifying holdings and if there are any changes to them. No new composite insurers are permitted. However, those already in existence may continue to write both life insurance and non-life insurance as long as each activity is separately managed. Contracts will be subject to a 14-30 day cancellation period and all relevant information should be provided both prior to and during the term of the contract.

Finally, once the directive was in place, Member States no longer needed to require prior approval or give systematic notification of rates or policy conditions. However, the home Member State may ask for some systematic

notification of the technical bases used for calculating scales of premiums and technical provisions, but only to verify compliance with Member State provisions concerning actuarial principles. Host Member States will be allowed to require non-systematic notification of policy conditions and other printed documents, but not scales of premiums. However, insurance contracts must adhere to the national legislation of the host Member State and to this end it could forbid the contract if it is contrary to national rights or public interest. Consequently, the Member State has a means of disallowing an insurance company the right to provide a cross-border service. To create a European market in insurance products, particularly life, further directives will be necessary and the bulk of Member State legislation harmonised. Each piece of legislation necessitated and created the next, and this process has formed the basis of the SEM's regulatory structure in insurance and financial services.

Spillover, Financial Services and European Integration

Neo-functional spillover alone cannot bring about harmonisation; it can only go so far without the impetus of further intergovernmental spillover in terms of further political treaties. However, the necessity of further treaties is created through neo-functional spillover and the realisation of the four freedoms. In these terms, neo-functional spillover is a functional variable within the integration process. It could be argued that the attainable legislation in financial services has been reached in this period of integration and if further neo-functional spillover is to be achieved greater intergovernmental spillover is necessary. The thesis argues that there is an interplay between intergovernmental and neo-functional processes and further intergovernmental spillover was realised in the Maastricht Treaty. Indeed, the actuality of the SEM and the environment for EMU allows neo-

functional spillover to take place. However, further treaties (intergovernmental spillover) will be necessary to create the environment for further harmonisation (neo-functional spillover) in the process of European integration.

The Spillover Model (pp 277-81) illustrates this process: intergovernmental spillover is indicated in the left hand column and is made up of intergovernmental agreements and neo-functional spillover is illustrated on the right hand side of the model. As explained above, neo-functional spillover constitutes three processes and each figure attempts to clarify these. The crosses on the model represent pieces of legislation that have been passed in relation to the Treaties that existed at that time e.g. X1 relates to the reinsurance directive and X2 the coinsurance directive. Indeed, the model, in line with this chapter, attempt to illustrate a spillover process in the context of European integration.

A SEM in financial services is intrinsically tied to the need for a single currency. However, whether EMU will materialise is debatable. One may only draw tentative conclusions about what the future situation entails. The Germans and French believe that stage three of monetary union is still on course and there are those who will be ready to make the transference. Yet there maybe those who are either unready or unwilling. In this context a two-speed Europe is not difficult to envisage. How the difference between being in the 'slow lane' or the 'fast lane' will affect the financial service sectors in the specific Member States remains to be seen. However, one cannot help thinking that the 'fast lane' may be more advantageous. To this end, it could be envisaged that a Member State financial services industry would want its government to ensure early entry.

Delors and the Commission ". . . portrayed EMU as functionally linked to the internal program and necessary for its success. . . . The August 1990 EC Commission document, Economic and Monetary Union . . . declares: A single currency is the natural complement of a single market. The full potential of the latter will not be achieved without the former" (Sandholtz, 1994; p 274). Indeed, " . . . the argument is that complete capital liberation . . . and exchange rate stability (in the EMS) are incompatible with divergent national monetary policies. It is illogical to expect that the EU can have; a single market, a fixed exchange rate, liberal capital movements and autonomous national monetary policies. Something must give because the " . . . first three bring about gains in efficiency . . . the submersion of national monetary policy autonomy in a European monetary policy" (ibid, p 276) becomes imperative. However, there are two major problems with the spillover thesis. Firstly, the functional link is not clear, a SEM could function without a single currency. Effectively, there is little consensus on the desirability of EMU let alone its necessity. Secondly, if the neo-functional theory of spillover is to hold, then ". . . once an integrative step has been taken, actors discover that they must integrate further in order to realise benefits. In the case of EMU, that kind of learning cannot have taken place. . . . The learning process postulated by neo-functionalists has not had time to occur" (ibid).

These are valid points. However, it would be ludicrous to consider that the initiation and pursuit of a SEM had nothing to do with EMU.

The 1992 programme produced a . . . positive attitude toward the EC, was fertile soil for the EMU initiative. . . . It bears remembering that the goal of monetary union had been established at the Hague summit in 1969, yet the EC made no real progress in that direction in the 1970s. The member states

reaffirmed monetary union as their objective at the creation of the EMS in 1979, but in succeeding years they failed to take any of the steps foreseen to achieve it. In 1988 and 1989, however, EMU became a movement. What had intervened was the 1992 project (ibid, 277).

Without the SEA and SEM, monetary union would not have reached the agenda. The SEM gave the EU credibility. Sectors realised the potential of the market which together ". . . increased the credibility of the community as a source of solutions to common problems" (ibid, p 276).

One may contend that economic sectors and political institutions perceive regulatory structures as externalities that affect their behaviour. However, it can be argued that a sector's and institution's behaviour both affect the regulatory environment and that they are subsequently affected by it; that there is a constant interaction between the two. Indeed, as illustrated above, this thesis has analysed the differing regulatory environments within the individual Member States and the legislation that displays how such differences may be discerned (see Life Insurance Regulation Matrices Chapter Five p 157 and 160).

One may consider that legislation is a dynamic element of the integration process. In the USA, interest groups consider that the best means of government intervention is at the federal rather than state level. This is because legislative disharmony would create a fragmented market (Dehousse 1991). In 1997, the EU life insurance market was still fragmented (although the application of the Third Life Assurance Directive is changing this) and it may be considered that the support for removal of trading barriers indicates

support by the sector for the SEM. But, at what cost in respect of their changing regulatory environments?

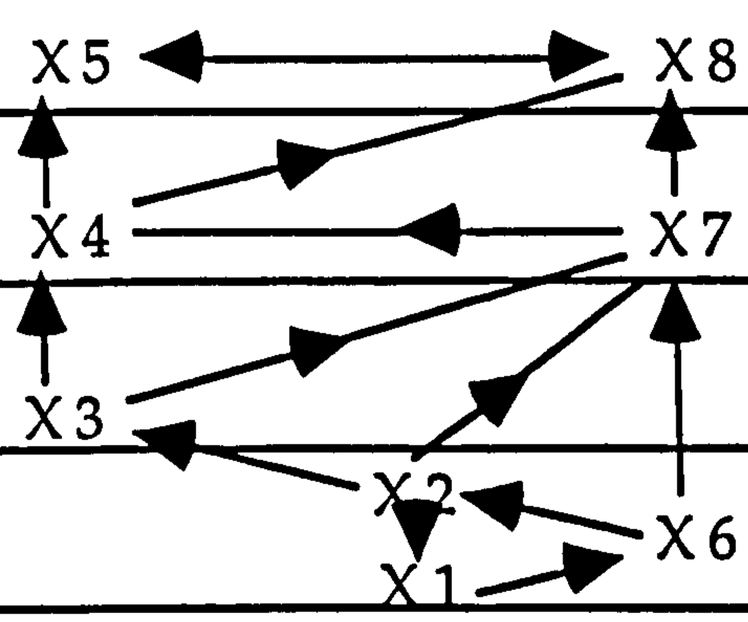
Conclusion

It could be posited that by the early 1980s financial services legislation had reached an impasse and that without the impetus of greater integration that the SEA allowed, the harmonisation process would have slowed down considerably. However, even with Maastricht, it is now apparent that only the less problematic areas of harmonisation have been achieved in the existing phase of integration. If a SEM in financial services is to be realised, further harmonisation will be necessary. As the Treaties indicate, single markets in banking and insurance are closely linked to the free movement of capital. However, to achieve the free movement of capital, one may contend that a single currency is essential and until this exists the idea of free capital movement is unrealistic. Only once monetary union has been realised can taxation and pension issues be discussed in detail and compromises pursued; only in the realisation of the Maastricht Treaty and EMU (intergovernmental spillover) will neo-functional spillover be intensified.

This thesis argues that there are two processes of spillover at work; one at a state level and one at a supranational, sector and interest group level. The former may be identified as intergovernmental spillover, the latter as neo-functional spillover. The latter may be broken down into three areas: general horizontal spillover (sector to sector or services to capital etc); specific horizontal spillover (insurance to banking i.e. sector bound); vertical spillover (within insurance i.e. industry bound). Finally, the difficulties outlined above may be perceived in the pursuit of creating a single market in insurance and particularly in life insurance. Chapters Five, Six and Seven

discussed the problems involved in the negotiations that created the Third Life Assurance Directive and showed how agreement may have been impossible without QMV and the SEM. The need for interest groups, supranationality and both forms of spillover in the integration process suggests that integration is not simply driven by intergovernmental processes, but by neo-functional processes as well. Indeed, through generalising this decision-making process Chapter Eight posits a theory of spillover (that incorporates aspects of both intergovernmentalism and neo-functionalism) that provides an understanding of European integration.

FIG 8.1

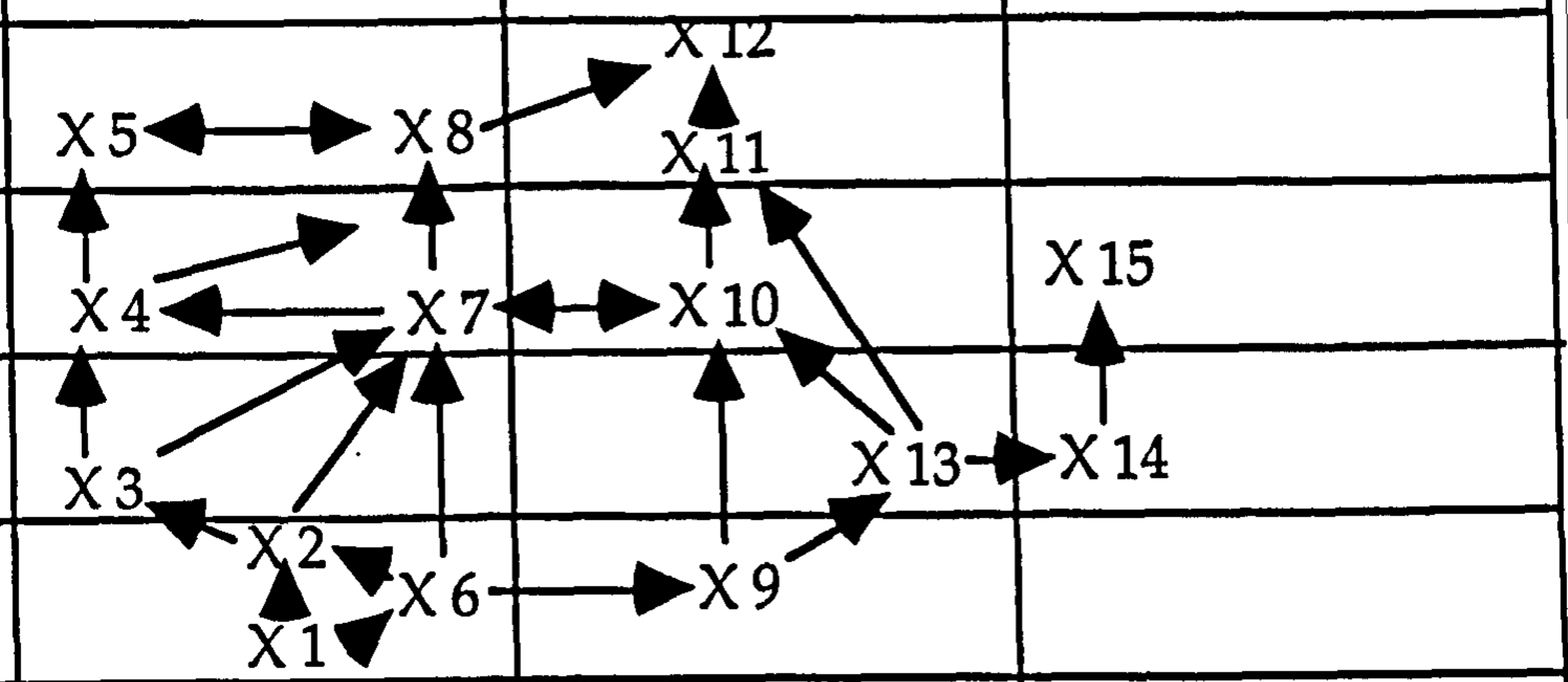
Intergovernmental Spillover	NEO-FUNCTIONAL SPILLOVER VERTICAL SPILLOVER (WITHIN SAME INDUSTRY)
EPU ?	
EMU 1999	
SEM 1992	
SEA/QMV 1987	
Direct Elections 1979	
EEC/Euratom 1957	
ECSC 1951	
	INSURANCE

Neo-Functional Spillover. Vertical Spillover (Within Same Industry)

X1. Re-insurance Directive 64/225/EEC
X2. Co-insurance Directive 78/473/EEC
X3. First Life Assurance Directive. 79/267/EEC
X4. Second Life Assurance Directive. 90/ 619/EEC
X5. Third Life Assurance Directive. 92/96/EEC
X6. First Non-Life Insurance Directive. 73/239/EEC
X7. Second Non-Life Insurance Directive. 88/357/EEC
X8. Third Non-Life Insurance Directive. 92/49/EEC

FIG 8.2

Intergovernmental Spillover	NEO-FUNCTIONAL SPILLOVER HORIZONTAL SPECIFIC SPILLOVER (INDUSTRY TO INDUSTRY (WITHIN SAME SECTOR)		
EPU ?			
EMU 1999			
SEM 1992			
SEA/QMV 1987			
Direct Elections 1979			
EEC/Euratom 1957			
ECSC 1951			
	INSURANCE	BANKING	PENSIONS



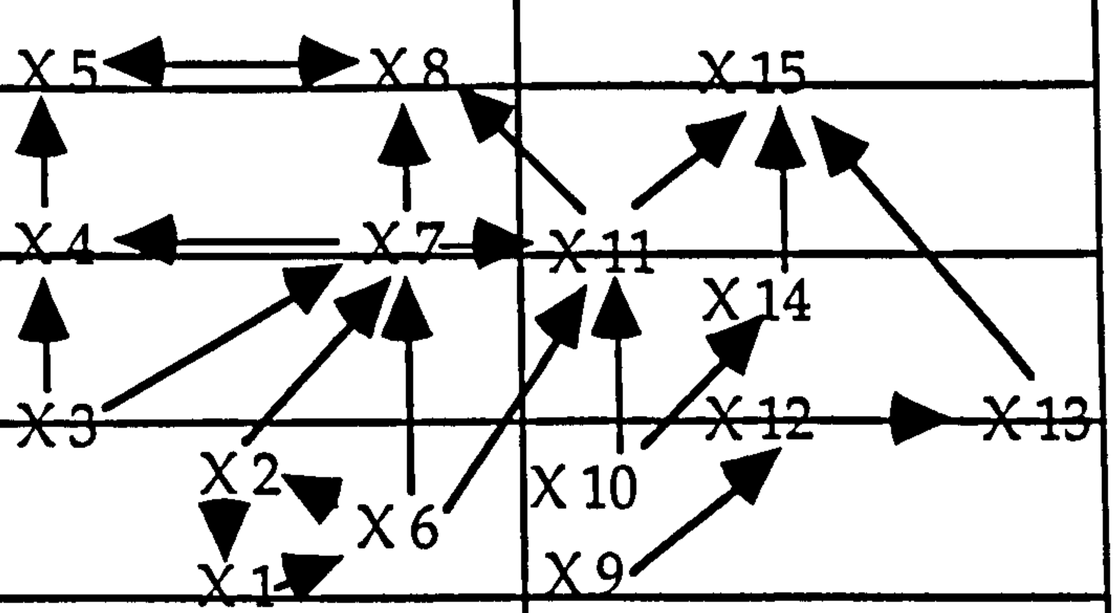
Horizontal Specific Spillover (Industry to Industry Within the Same Sector)

X1. Re-insurance Directive 64/225/EEC
X2. Co-insurance Directive 78/473/EEC
X3. First Life Assurance Directive. 79/267/EEC
X4. Second Life Assurance Directive. 90/ 619/EEC
X5. Third Life Assurance Directive. 92/96/EEC
X6. First Non-Life Insurance Directive. 73/239/EEC
X7. Second Non-Life Insurance Directive. 88/357/EEC
X8. Third Non-Life Insurance Directive. 92/49/EEC

X9. First Banking Directive. 77/780/EEC
X10. Second Banking Directive. 89/646/EEC
X11. Capital Adequacy Directive. 93/6/EEC
X12. Solvency Ration Directive. 94/7/EEC
X13. Accounts Directive for Banks and Other Credit Institutions.
X14. Directive Concerning Equal Treatment for Men and Women in Occupational Social Security Schemes. 86/378/EEC
X15. Directive Concerning the Rights of Residence for Self-Employed Persons Who have Ceased Occupational Activity. 90/365/EEC

FIG 8.3

Intergovernmental Spillover		NEO-FUNCTIONAL SPILLOVER HORIZONTAL GENERAL SPILLOVER (SECTOR TO SECTOR)	
EPU ?			
EMU	1999		
SEM	1992		
SEA/QMV	1987		
Direct Elections	1979		
EEC/Euratom	1957		
ECSC	1951		
		SERVICES	CAPITAL



Horizontal General Spillover (Sector to Sector)

X1. Re-insurance Directive 64/225/EEC
X2. Co-insurance Directive 78/473/EEC
X3. First Life Assurance Directive. 79/267/EEC
X4. Second Life Assurance Directive. 90/ 619/EEC
X5. Third Life Assurance Directive. 92/96/EEC
X6. First Non-Life Insurance Directive. 73/239/EEC
X7. Second Non-Life Insurance Directive. 88/357/EEC

X8. Third Non-Life Insurance Directive. 92/49/EEC
X9. Abolition of Restrictions to Freedom of Establishment and Services Directive (regarding self-employed activities of banks and other credit institutions). 73/183/EEC
X10. First Banking Directive. 77/780/EEC
X11. Second Banking Directive. 89/646/EEC
X12. Stock Exchange Admissions Co-ordination Directive. 79/279/EEC
X13. Securities Admissions Directive. 93/22/EEC
X14. UCITS Directive 85/611/EEC
X15. Investment Services Directive 93/22/EEC

Chapter Nine

Conclusions: Constructing a Substantive Theory

> *What, then, is Europe? It is a kind of cape of the old continent, a western appendix to Asia. It looks naturally toward the west. On the south it is bordered by a famous sea whose role, or should I say function, has been wonderfully effective in the development of the European spirit with which we are concerned (Valery, 1962; pp 311-312)).*

Introduction

This thesis has heeded the calls for empirical studies regarding European integration theory. Through an analysis of the European life insurance industry, it has constructed a substantive theory to enhance our understanding of European integration. This substantive theory joins the hierarchy of substantive/formal theories in the area of integration. It is a theory which questions and adds to neo-functionalism and intergovernmentalism, and ultimately identifies elements of both in the process of European integration. Indeed, it adds to the formal theories and posits that certain parts may be fused to further our comprehension of European integration processes. The thesis pursued a grounded theory understanding of theory which considers that a theory's only replacement is another theory, that theories are modified rather than proved. In this context, the thesis's ontology was *critical realist* in outlook (taking the view that reality does exist beyond human construction but the human intellect is

flawed and unable to comprehend it perfectly). Indeed, the inquiry paradigm was *postpositivist* (Guba and Lincoln 1994).

Theory Building

Grounded theory techniques have been employed in the following ways. Firstly, *open coding* of *concepts* was undertaken through the *categorisation* of individual Member States' life insurance legislation and regulatory regimes. This allowed *properties* and *dimensions* to be identified which provided the basis of a regulation table and matrix. Indeed, categories emerged through the *open sampling* of the data. Further coding and sampling through a survey of Member State insurance industries refined the matrix. Coding at this point was primarily open, however, *axial coding* had begun to relate the *categories* and *subcategories* more specifically and indicate possibilities of *process*. In this context, sampling began to focus on the *validation* of the *categories* and the relationships between them. The validated table (Table 2.1) and matrix (Fig 5.2) raised questions with regard to how legislative differences between Member States may be resolved. Through *axial coding* and *selective coding*, further interaction and process were identified and illustrated through the European Decision-Making Model. Initially the sampling was relational and variational, however it soon became more *discriminate* and pin-points those individuals that needed to be interviewed and identified the need for a further survey. Each part of the *theoretical coding* and *sampling* added to the tables, matrix and models which provide the building blocks of the substantive theory.

The *selective coding* process is specifically illustrated by the matrix and the model fitting together around the *core category* of European integration Indeed, *sub-categories* the SEM, regulatiory environments, compromise and

the EU fit around the *core category* and provide the *story-line*. *Axial coding* draws all parts of the analysis together and it is the pivot or the axis of theory building. Selective coding identifies the *core category* and develops the *core category* in relation to *sub-categories*. Indeed, *open, axial* and *selective coding* interact in the process of theory building. This is illustrated through the Spillover Model, which extrapolates the process of legislation formulation identified in the European Decision-Making Model and postulates both neo-functionalism and intergovernmentalism in the process of European integration. Indeed, the generalisation is one usually employed in qualitative methodology i.e. from one setting to others. This provides high validity but low reliability. Furthermore, the four central criteria (*fit, comprehendability, generality and control*) of substantive theory are met in the theory building process. The theory draws on diverse data and attempts to be true to the reality under scrutiny (it should *fit*). Secondly, the *fit* should be made *comprehendable*. This has been achieved through using tables, matrices, models and diagrams to make the findings of the research process explicit. Thirdly, from the diverse data certain *generalisations* are made. However, the research makes clear the limitations of these *generalisations* and clarifies when the conditions apply to specific situations, there is *control*.

In this context, substantive theory is formulated in relation to the formal theories of intergovernmentalism and neo-functionalism. Indeed, through grounded theory techniques a substantive theory is built to give an understanding of European integration and allow a greater comprehension of European integration, the SEM, and the European Union. Through *open coding* and comparative analysis the need for a survey is initiated (induction); this provides a deduction which considers that to create an SEM Member States need to compromise their normative regulatory environments; this

provides *selective coding* which indicates further induction through *axial and selective coding.*

Finally, these procedures illustrate the need for a further survey which allows for data saturation and an in-depth understanding of the phenomenon. Throughout the analysis induction and deduction go hand-in-hand. The researcher is continually analysing the data in the process of building theory and continually challenging theory through collecting and analysing data. Indeed, ". . . methodology is the theory of methods . . . (and the) . . . grounded theory methodology is in itself a theory which is generated alongside substantive theory it is generating" (Glaser, 1992; p 7 author's brackets).

The substantive aspects of the theory have built up an understanding of the processes of integration through an analysis of decision-making. This illustrated how Member States as political units were losing control over the creation of legislation and their subsequent sovereignty. The benefits of being a member of the EU are illustrated against these losses in terms of greater profitability and the consequent necessity of ensuring market conditions to maximise this. In this way, a calculation of benefit or loss may be posited. Ultimately, one may determine the rationale behind membership of the EU and the extent to which sovereignty may or may not be surrendered. Neo-functionalism (a formal theory) is one of incremental integration through the transfer of allegiance to a supranational body, the use of interest groups and the concept of spillover. On the other hand, intergovernmentalism (another formal theory) considers that the nation-state is the main impetus behind the European integration process. The substantive element of the theory formulated in this thesis assesses to what extent the formal theories are supported by the evidence.

If sectors/industries (in this case, the insurance industry) are involved in the construction of the SEM and furthering European integration, then the process is not purely intergovernmental (or state-centric): other actors are involved. However, as the Council of Ministers passes legislation, an intergovernmental element still remains quite strong. But even at this level,

> . . . state executives do not determine the European agenda because they are unable to control the supranational institutions they have created at the European level. The growing diversity of issues on the Council's agenda, the sheer number of state executive principals and the mistrust that exists among them, and the increased specialisation of policy-making have made the Council of Ministers reliant upon the Commission to set the agenda, forge compromises, and supervise compliance. . . . Policy-making in the EU is characterised by mutual dependence, complementary functions and over-lapping competencies (Marks *et al*, 1996a; p 372)

The substantive theory developed here considers that industries/sectors compromise their own interest at the EU level (this is achieved through national interest groups, e.g. the ABI, and European interest groups, e.g. the CEA). This too illustrates aspects of neo-functionalism as the use of interest groups, particularly European interest groups, is central to a neo-functional understanding of European integration. Compromise between the EU-wide sector/industry and the Commission is reached primarily through European interest groups. The use of EU-wide interest groups is emphasised in the interaction and compromises that are reached between the EU legislative bodies and the EU-wide interest groups in the creation of European legislation. However, the national interest groups still play an important role

in the process by reporting back to national governments. In general, the substantive theory concludes that there has been a shift in allegiance from the national legislature to the EU with regard to certain issues. However, the Member States still played an important role in the decision-making process. Indeed, through multi-level governance, there has been a shift toward joint sovereignty in the creation of EU legislation. This is illustrated through the concepts of intergovernmental and neo-functional spillover; the former creates the environment through the Treaties, whereas the latter pushes this forward through the need for industries/sectors to ensure their advantage in the evolving EU. This process initiates a shift away from economic interdependence toward an intensification of integration, a move away from intergovernmental process of integration toward neo-functional. Not simply state-centric governance, but governance of a multi-level nature. Governance that illustrates a shift in sovereignty. "In practice, the erosion of national sovereignty means the erosion of the power of the Member States to decide exclusively much of their public policy. . . . Empirically, it is beyond dispute that the EU level is now the level at which a high proportion (possibly 60 per cent) of what used to be regarded as purely domestic policy-making takes place . . . therefore power has shifted. A much more complex structure of policy-making has developed" (Richardson, 1996a; p 3).

Formal Theories

Neo-functionalism is grounded in Kantian political thought and considered peace-oriented in terms of a specific region. It is a peaceful process directed at a peaceful end and wishes to ensure a 'civic constitution' under the auspices of perpetual peace (Kant 1995). Neo-functionalism proposes that the EU is a supranational entity which through its growing authority encourages the transferral of allegiance away from national institutions and towards the

European. The main body of the research in this thesis investigates whether such a process is at work in the creation of the SEM through grounded theory techniques and an empirical study of a specific sector. It considers that, unlike federalism, the neo-functional supranational entity is a step towards functional ends, i.e. that supranationality is a process and an element in a transformation away from the nation-state toward an international entity. Indeed, it is considered, that the dynamism of this process is spillover and the enhancement of supranationality.

On the other hand, intergovernmentalism argues that the nation-state is central to the process and will remain so. "The intergovernmentalist argument implies that states form their preferences via some hermetic national process, then bring those interests to Brussels. The implication is that EC institutions have no impact on the formation of state interests" (Sandholtz, 1994; p 260). Indeed, the interviews and the European Decision-Making Model illustrate that ". . . national interests of EC states do not have independent existence; they are not formed in a vacuum then brought to Brussels. . . . States define their interests in a different way as members of the EC than they would without it" (ibid). However, this thesis acknowledges that through intergovernmental spillover the environment for further and more intensive neo-functional spillover is created. This again allows an extension in supranational decision-making.

The empiricism is bound up in the changes that are taking place as the EU evolves, especially now that the process has intensified. Indeed, the idea of neo-functional transformation has re-emerged (in the aftermath of the SEA, the SEM and the plans for EMU) and the evolving EU is where the process may be further identified and best observed. As Haas pointed out,

> . . . for the political scientist the unification of Europe has a peculiar attraction quite irrespective of merits and types. He may see it, as I do, an instance of voluntary 'integration' taking place before his eyes, as it were under laboratory conditions. He will wish to study it primarily because it is one of the very few current situations in which the decomposition of old nations can be systematically analysed within the framework of the evolution of a larger polity, perhaps, to develop into a nation of its own (Haas, 1958; p xxxi).

This thesis proposes that through the political impetus of the SEA (1987) the harmonisation of legislation and regulation, as pointed out by Cecchini (1986), is being reformed to meet what is considered the normative conception of the evolving SEM. However, it also proposes that the normative concept of the SEM is tempered by the ideas that the industries have of their own trading structures and that these will differ from one Member State to the next, because each is acclimatised to trading in a specific regulatory environment. Such has been indicated by the results of the European survey and is explicit in the Third Life Assurance Directive, with reference to both the process of formulation and the end result (as indicated through the interviews). This allows the author to suggest that both supranational and spillover tendencies are at work.

(a) Supranationality is observed in terms of industry's interaction with the EU's institutions and the creation of the legislation that makes further interaction necessary, i.e. directives and further treaties.

(b) Spillover is observed in terms of the need for further legislation in the European life insurance industry and other financial services (non-life

insurance, banking and pensions) and sectors (capital) related to it. It is suggested that EMU will intensify the need for harmonisation in these areas and it is in this context that intergovernmental and neo-functional processes can be observed. In intergovernmental terms, spillover can be seen in the creation of the Treaties and agreements that further integration i.e. ECSC, EEC, Enlargement, Direct Elections, SEA, SEM, EMU. While in neo-functional terms, spillover may be observed in three areas (a) in one industry (the insurance industry) *vertical spillover;* (b) spillover from industry to industry (from insurance to banking) *horizontal specific spillover* and; (c) from sector to sector (from services to capital) *horizontal general spillover* (see Figures 8.1, 8.2 and 8.3 pp 277-81).

The argument is emphasised by Sandholtz (1994) who considers that 1992 ". . . increased the level of support, among publics and political leaders, for EC-level initiatives. Widespread enthusiasm for the 1992 project tilted preferences toward programs that could be seen as cementing the gains from the single-market program" (p 274). This was a case of spillover in that ". . . integration in one issue area would reveal functional linkages to other issue areas; as a result, the desire to obtain the full benefits of integration in the first area would lead to pressure for integration in a second, linked sector" (ibid, pp 274-275). However, spillover, as deterministic process toward greater integration was criticised and ". . . theorists wrote about 'spill-backs' and 'spill-around.' What was not refuted was the notion that spillovers could occur; indeed, if issues are linked, then the potential for spillovers always exists. The process is simply not automatic or one directional" (ibid, p 275).

Overall, the thesis has identified a number theoretical propositions suggested by neo-functionalism through an empirical analysis of the Member States life insurance industries and the EU's decision-making processes. The survey

proposes that differences exist between the Member state concepts of the best regulatory environment. At some point, these differences needed to be resolved if the European life insurance industry was to be unified in what was considered to be the best regulatory environment for the industry as a whole. In its negotiations with the Commission there needed to be some common ground if the legislation being formulated was not supported by enough of the Member State industries, it could be blocked at the Council level. In this context, there is a need to negotiate with the supranational body through the use of European interest groups to ensure successful legislation and, through compromise, the most comfortable trading conditions. Through the need to be involved in the decision-making process, one may consider that supranationality and spillover are at work. The need to ensure regulatory conditions as similar as possible to one's own forces Member State industries/sectors and governments to become further and further involved in the integration process.

As the free movement of services is being attempted and monetary union is no longer perceived as unattainable, more and more difficulties become apparent. Consequently, it becomes ever more necessary for Member States to make mutual concessions. Compromise becomes the central factor and any national assertion in the face of the need for pragmatism slows up or destroys the process. However, as the process becomes more intense, agreements are harder to win, as Lindberg argued,

There is no paradox between the progress of economic integration in the Community and sharpening political disagreement; indeed, the success of economic integration can be a cause of political disagreement. The Member States are engaged in the enterprise for widely different reasons, and their actions

> have been supported or instigated by elites seeking their own particular goals. Therefore, conflicts would seem endemic as the results of joint activity come to be felt and as the pro-integration consensus shifts (Lindberg, 1963; p 80).

These conflicts may be illustrated through the intergovernmental role in the integration process. As international difficulties with regard to European competitiveness became paramount, pressure was put on governments by industries/sectors to further a common market in Europe. This created the necessity to agree the SEA and the Maastricht Treaty at the Member State level, and indicated the part played by industries/sectors in pursuing self-interest.

The SEA, the SEM and the Maastricht Treaty create clarity of objectives and what is necessary if these objectives are to be realised. It also becomes necessary for each area to be looked at in the context of its own specifics and this necessitates the involvement of interest groups and sectors. The sword is double edged: what needs to be changed becomes clearer but winning these changes becomes harder. However, clarity negates Haas' "turbulence" and creates "wholes". It provides for "focal points" and "shared belief systems" (Garrett *et al*, 1993; p 176).

The knowledge of national trading structures and what is necessary for harmonisation (focal points) negates turbulence. Working parameters are drawn up by the actors involved and, through the neo-functional processes of spillover and supranationality, compromise is reached and integration intensified. However within the process, there is an intergovernmental element, i.e. the Council of Minister's and the sectors' interaction with national governments, but as integration intensifies this aspect of the process

diminishes and Morganthau's understanding that political change will be linked to its historical circumstances is verified (Morganthau, 1973). Indeed, the process of integration is neither purely intergovernmental nor totally neo-functional, but as has been illustrated, an amalgamation of both and in this context it carries elements of realism and functionalism.

Neo-functionalism is at work in the process of European integration. It is a peaceful process looking toward a peaceful end. However, the actual end cannot be foreseen. Indeed, can any end be categorically stated? With regard to European Union one may question what Europe actually is. Where does it end? Neo-functionalism could be seen as a step in the direction of an international civic constitution and could be seen as a means of attaining a functional end.

The Substantive Theory

As outlined above, the substantive theory is built through *coding*, *categorisation* and *process*. The regulation table and matrices provide the basis of the substantive theory in that they acknowledge that separate Member States pursue different regulatory regimes. This sets up the problem of understanding how compromise is reached. The interviews, observations and survey C further construct the substantive theory with regard to the EU decision-making process. This substantive theory has implications for the formal theories of intergovernmentalism (state-centric governance) and neo-functionalism (multi-level governance) in terms of spillover, supranationality and interest group utilisation.

"A substantive theory generated from the data must be formulated, in order to see which of diverse formal theories are, perhaps, applicable for furthering

additional substantive formulations" (Glaser and Strauss, 1967; p 34). This illustrates that theories are never complete but processes in themselves. In this context, one may question the extent to which neo-functionalism may be labelled a formal theory, and question the extent to which it is a substantive theory of integration theory in that it has not really emerged from studies under different types of situations i.e. integration processes external to western Europe. Indeed, one may question the extent to which neo-functionalism or intergovernmentalism may be labelled formal theories.

The substantive theory is illustrated by the table, scale, matrices and models that have been built by the on-going research (see below) and from it a number of conclusions may be drawn. Diagrams are a fundamental aspect of grounded theory, they allow a visual representation of the substantive theory and illustrate the relationships between the concepts and how different parts of the research relate to one another.

Regulation and Legislation Table (Table 2.1) p 43.

Regulation Scale (Table 5.1) p 138.

Life Insurance Regulation Matrix One (Figure 5.1) p 157.

Life Insurance Regulation Matrix Two (Figure 5.2) p 160.

Easton' s Amended Demand Flow Model (Figure 7.1) p 214.

The European Demand Model (Figure 7.2) p 215.

The European Decision-Making Model (Figure 7.3) p 243.

The Spillover Model (Figures 8.1, 8.2 and 8.3) pp 277-81.

Indeed, the substantive theory itself may be summarised in the following way:

(a) Sectors/industries (in this context the life insurance industry) are involved in the construction of the SEM and consequently further and intensify European integration.

(b) They participate in the decision-making process in a number of ways but primarily through the use of national and European interest groups.

(c) Each Member State's sector/industry compromises its own interest at the EU level (this is achieved through national interest groups, e.g. ABI, and European interest groups, e.g. CEA).

(d) Compromise between the EU-wide sector/industry and the Commission is reached primarily through European interest groups.

(e) Compromise between the EU legislative bodies, national legislatures and interest groups takes place throughout the creation of European legislation.

(f) There is a shift in allegiance (by the national sector industry) from the national legislature to the EU with regard to certain issues. However, the Member States still play an important role in the decision-making process. Indeed, there has been a shift toward joint sovereignty in the creation of EU legislation. Through this process integration is intensified.

(g) The intensification takes the form of spillover in intergovernmental and neo-functional terms. This creates the impetus for further integration.

(h) European integration is given impetus by economic industries/sectors pursuing their self-interest in the creation of EU legislation. However, this allows welfare for Europeans in terms of greater prosperity and peaceful co-existence. Again, this intensifies European integration.

European integration is the *core-category* and the impetus for the interaction between Member States and sectors. An interaction that has been identified through *open, axial and selective coding.*

As mentioned above, the substantive theory was constructed through an induction/deduction process. The inductive element encompassed the creation of a table and matrices through coding and categorisation. This was added verified and enhanced by a survey. This led to a number of deductions which initiated further inductive research through a series of semi-formal interviews. Once again, this created further deductions which were verified by another survey. In practical terms, this meant that through the construction of the table and matrices, we discover that different Member States pursue different concepts of a regulatory environment. Ultimately, this led the thesis to question how Member States overcome their differences. The interviews provided an understanding of how compromise is pursued and indicated some generalisations.

Finally, the substantive theory identifies that a multi-level understanding of governance is apparent at the EU level. This does not mean that the Member State is not involved, but it does indicate the difficulties with a purely state-centric view.

> Multi-level governance does not confront the sovereignty of states directly. Instead of being explicitly challenged, states in the European Union are being melded gently into a multi-level polity by their leaders and by the actions of numerous sub-national and supranational actors. State-centric theorists are right when they argue that states are extremely powerful institutions that are capable of crushing direct threats to their existence. The organi(s)ational form of the state emerged because it proved an effective means of systematically wielding violence. . . . One does not have to argue that states are on the verge of political extinction to believe that their control of those living in

their territories has been significantly weakened (Hooghe and Marks, 1997; p 38 author's bracket).

The interviews suggested that in some cases state executives are unable to hold onto sovereignty. Indeed, collectively they are unable to define the agenda ". . . because they are unable to control the supranational institutions they have created at the European level" (ibid). Sectors (sub-national actors) circumvent the national legislature and directly lobby the EU institutions. It is apparent that decision-making at the European level ". . . is characterised by mutual dependence, complementary functions, and overlapping competencies" (ibid). Thus, there is an interaction between intergovernmental and neo-functional processes at the EU level. During the 1960s and the 1970s, an intergovernmental system was in the ascendance and this provided the environment for the state-centric model. However, with the advent of the SEA in the 1980s and the added authority of the EU institutions ". . . a system of multi-level governance arose, in which the activities of supranational and sub-national actors diluted national government control" (ibid, p 39). The interviews illustrated that the Member States were ". . . no longer . . . the exclusive nexus between domestic politics and international relations" (ibid). Indeed, sub-national actors were making ". . . direct connections . . . in diverse political arenas. Traditional and formerly exclusive channels of communication and influence are being side-stepped" (ibid). Multi-level governance allows interest groups to be involved at both EU and national levels. However, as the interviews and subsequent Decision-Making Model illustrated, when we speak of European legislation, the shift is toward the supranational.

The SEA and the Maastricht Treaty have led to discussions around the concept of sovereignty. "Several member-state governments, are themselves

deeply riven on the issues of integration and sovereignty. States and state sovereignty have become objects of popular contention - the outcome of which is as yet uncertain" (ibid, p 40).

Further Research

This thesis has reassessed the general literature on integration theory in an effort to allow a greater understanding of the process of European integration. Indeed, it has approached the subject matter through the methodology of grounded theory. This has allowed the author to overcome a number of problems identified with neo-functionalism. Grounded theory identifies the difficulties inherent in qualitative analysis and considers that there is no need to attempt to copy the quantitative process, usually the scientific method. There is no need for theory simply to predict and, in doing so, identify a dependent variable. Ultimately, theory should enlighten and this can be done by enabling understanding. This has been the objective of this thesis, to provide further understanding of European integration processes in general and neo-functionalism and intergovernmentalism in particular. As indicated above the methodology was based on a *postpositivist* paradigm of inquiry. Indeed it considered that there is a reality external to humanity and that this may be imperfectly comprehended through recognising subjectivity in the pursuit of objectivity. However, during the analysis the author considered that if one's metaphysical beliefs leaned toward the ontology of historical realism (reality shaped by social, historical, ethnic economic or gender values and concretised over time) grounded theory and neo-functionalism could be perceived as *critical theories* of the prevailing historical realism's. On the one hand, the nation-state (an established historical phenomenon in institutional terms) and on the other *positivist* and *postpositivist* (established methodologies) modes of analysis. Indeed, grounded theory could be

understood as a dialectical shift between the paradigms of inquiry i.e. between *postpositivism* and *critical theory*. More research in terms of methodological processes may allow insights into the theories that provide further explanation and understanding of the European integration process. (Guba and Lincoln, 1994; and Annells, 1996).

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APPENDICES

Appendix A
Surveys

Survey A

A Survey of the European Life Insurance Industry

(1) How liberal or state controlled is your national life insurance market?

(2) Where would you place the Single European Market (SEM) life insurance sector in respect of regulatory freedom?

(3) What type of regulatory environment do you consider that the SEM should be to allow your company its greatest advantage?

(4) What type of regulatory environment do you consider the SEM in life insurance should be to allow the greatest consumer protection?

(5) What type of regulatory environment do you consider the SEM in life insurance should be to allow the greatest consumer choice?

(Respondents were asked to give their answers on the regulation scale of 1-12 which was fully explained to them)

Survey B

General Survey of Institutions involved in the Decision-Making Process

(1) How liberal or state controlled is your national life insurance industry?

(2) Where would your organisation's membership place the single European Market life insurance industry in respect of market freedom?

(3) What type of market would your organisation's membership consider that the Single European Market should be to allow the life industry its greatest profitability?

(4) What type of market would your organisation's membership consider that the Single European market should be to allow the greatest consumer protection?

(5) What type of market would your organisation's membership consider that the Single European Market should be to allow the greatest consumer choice?

Survey C

A Survey of the UK Insurance Industry Regarding Interest Group Usage.

(1) Your company used organised interest groups at the European level i.e. the CEA in the formulation of the Third Life Assurance Directive.

(2) Your company used organised interest groups at the national level i.e. the ABI in the formulation of the Third Life Assurance Directive.

(3) Your company uses organised interest groups at the European level for most European issues.

(4) Your company subscribes to a European interest group.

(5) Your company subscribes to a national interest group.

(6) Your company lobbies European institutions when its European interests are affected.

(7) Your company lobbies the national government when European interests are affected.

(8) Your company primarily uses interest groups to lobby on its behalf at the European level.

(9) Your company primarily uses interest groups to lobby on its behalf at the national level.

(10) Your company prefers to use interest groups at the European level because this allows European sector wide compromises.

(11) Your company prefers to use interest groups at the national level because this allows nation-wide sector compromises.

(Respondents were asked to give their answers on a Likert scale of 1-4)

Appendix B
Interview Questions/Outlines

The interviews were conducted on a semi-formal basis and centred and categorised around 12 core questions, these were:

Interest Group Interviews

(1) What are the major functions of the CEA/BIPAR/ABI and how do these fit in with the functions of other finance interest groups and governmental institutions at:

(A) The EU level?

(B) The national level?

(2) To what extent are decisions made with interest group input?

(3) Is it interest groups, the Council Ministers or the Commission that define decision parameters?

(4) Do the Council, the Commission, national legislatures and interest groups reach a compromise prior to a decision reaching the Council?

(5) Does an interaction exist between the Council and the specific interest group on a national and European level?

(6) How does the Council know what to insist upon in respect of national interest?

(7) Does an interaction exist between interest groups and the Insurance Committee?

(8) Are different Member states looking for specific types of life assurance market environment for the SEM which is different from other member states?

(9) Are there differences between the:

(a) The French market ideal?

(b) The German market ideal?

(c) The Dutch market ideal?

(d) The UK market ideal?

(e) The Italian market ideal?

How does your market ideal fit into these?

(10) Is a compromise reached between the different national interest groups prior to the Commission initially drawing up draft legislation or is there an interaction between the interest group at the European level and the Commission which takes into consideration a compromise reached by the member state interest groups i.e. ABI through membership of the European interest group CEA/BIPAR?

The COREPER Interviews

(1) What are the major functions of a Permanent Representative and how do these fit in with the functions of political institutions at:

(A) The EC level?

(B) The national level?

(2) To what extent are decisions made with interest group input?

(3) Is it interest groups, the Council Ministers or the Commission that define decision parameters?

(4) Do the Council, the Commission, National legislatures and interest groups reach a compromise prior to a decision reaching the Council?

(5) Does an interaction exist between the Council and the specific interest group on a national and European level?

(6) How does the Council know what to insist upon, in respect of national interest?

(7) Does an interaction exist between interest groups and the Insurance Committee?

(8) Are different Member States looking for specific types of life insurance market environment for the SEM which is different from other member states?
(Could you indicate these differences, please)

(9) Are Permanent Representatives aware of a set of parameters from which they must not stray in the decision making process? (Could you indicate how these are reached, please). How do interest groups fit into the process from a Council perspective?

(10) Is a compromise reached between the different national interest groups prior to the Commission initially drawing up draft legislation. Alternatively,

is there an interaction between the interest group at the European level e.g., the CEA, and the Commission which takes into consideration a compromise reached by the member state interest groups through their membership of the European interest group?

(11) Where possible, have compromises been reached between the Council, the Commission and Parliament before the final negotiations to enable a more efficient means of decision making?

(12) What takes precedence in the formulation of a Directive Member State or sector interests?

The Commission Interviews

(1) What are the major functions of the Commission and how do these fit in with the functions of interest groups at:

(A) The EU level?

(B) The national level?

(2) To what extent are decisions made with interest group input?

(3) Is it interest groups, the Council Ministers or the Commission that define decision parameters?

(4) Did the Commission, national legislatures and interest groups interact and reach a compromise prior to the Third Life Assurance Directive proposal reaching the Council?

(5) Does an interaction exist between the Commission and the specific interest group on a national (ABI) and/or European level (CEA)?

(6) How does the Commission know what to insist upon in respect of European interests i.e. in terms of insurance policy that is acceptable to all Member States?

(7) Does an interaction exist between interest groups and DG XV? Is this through the Insurance Committee (if so, how effective is the Insurance Committee)?

(8) Were different Member states looking for specific types of life insurance market environments for the Single European Market (SEM) which were different from other member states? (Could you indicate these differences please)

(9) Are there set parameters from which the Commission should not stray in the decision-making process? (could you indicate how these are reached please).

(10) Is a compromise reached between the different national interest groups prior to the Commission initially drawing up draft legislation or is there an interaction between the interest group at the European level, i.e. CEA, and the Commission which takes into consideration a compromise reached by the Member State interest groups, i.e. ABI, through membership of the European interest group?

(11) Where possible, have compromises been reached between the Council, the Commission and Parliament before the final negotiations to enable a more efficient means of decision-making?

(12) What took precedence in the formulation of the Third Life Assurance Directive, Member State, European (Commission) or life insurance industry interests?

The Supervisors Interviews (UK)

(1) What are the major functions of the DTI in the decision-making process and how do these fit in with the functions of other Government bodies at:

(A) The EU level?

(B) The national level?

(2) To what extent are decisions made with DTI input?

(3) Is it interest groups or the DTI, the Council of Ministers or the European Commission that define decision parameters?

(4) Do the Council, the Commission, national legislatures and regulators reach a compromise prior to a decision reaching the Council? How is this achieved?

(5) Does an interaction exist between the Council and the specific interest group on a national and European level prior to DTI input?

(6) How does the Council know what to insist upon in respect of national interest?

(7) Does an interaction exist between the DTI and the Insurance Committee?

(8) Are different Member States looking for specific types of life insurance market environments for the SEM which is different from other member states?

(9) Are their differences between the:

(a) The French market ideal?

(b) The German market ideal?

(c) The Dutch market ideal?

(d) The UK market ideal?

(e) The Italian market ideal?

Please illustrate these differences.

(10) Is a compromise reached between the different national interest groups prior to the Commission initially drawing up draft legislation or is there an interaction between the interest group at the European level, i.e. CEA, and the Commission which takes into consideration a compromise reached by the Member State interest groups, i.e. ABI, through membership of the European interest group? How does the DTI fit into the process?

(11) Where possible have compromises been reached between the Council, the Commission and Parliament before the final negotiations to enable a more efficient means of decision-making?

(12) What takes precedence in the formulation of a Directive, Member State or Industry interests?

Appendix C
The Third Life Assurance Directive

II

(Acts whose publication is not obligatory)

COUNCIL

COUNCIL DIRECTIVE 92/96/EEC

of 10 November 1992

on the coordination of laws, regulations and administrative provisions relating to direct life assurance and amending Directives 79/267/EEC and 90/619/EEC (third life assurance Directive)

THE COUNCIL OF THE EUROPEAN COMMUNITIES,

Having regard to the Treaty establishing the European Economic Community, and in particular Articles 57 (2) and 66 thereof,

Having regard to the proposal from the Commission (1),

In cooperation with the European Parliament (2),

Having regard to the opinion of the Economic and Social Committee (3),

1. Whereas it is necessary to complete the internal market in direct life assurance, from the point of view both of the right of establishment and of the freedom to provide services, to make it easier for assurance undertakings with head offices in the Community to cover commitments situated within the Community;

2. Whereas the Second Council Directive 90/619/EEC of 8 November 1990 on the coordination of laws, regulations and administrative provisions relating to direct life assurance, laying down provisions to facilitate the effective exercise of freedom to provide services and amending Directive 79/267/EEC (4) has already contributed substantially to the achievement of the internal market in direct life assurance by granting policy-holders who, by virtue of the fact that they take the initiative in entering into a commitment with an assurance undertaking in another Member State, do not require special protection in the Member State of the commitment complete freedom to avail themselves of the widest possible life assurance market;

3. Whereas Directive 90/619/EEC therefore represents an important stage in the merging of national markets into an integrated market and that stage must be supplemented by other Community instruments with a view to enabling all policy-holders, irrespective of whether they themselves take the initiative, to have recourse to any assurer with a head office in the Community who carries on business there, under the right of establishment or the freedom to provide services, while guaranteeing them adequate protection;

4. Whereas this Directive forms part of the body of Community legislation already enacted which includes the First Council Directive 79/267/EEC of 5 March 1979 on the coordination of laws, regulations and administrative provisions relating to the taking up and pursuit of the business of direct life assurance (5) and Council Directive 91/674/EEC of 19 December 1991 on the annual accounts and consolidated accounts of insurance undertakings (6);

5. Whereas the approach adopted consists in bringing about such harmonization as is essential, necessary

(1) OJ No C 99, 16. 4. 1991, p. 2.
(2) OJ No C 176, 13. 7. 1992, p. 93; and Decision of 28 October 1992 (not yet published in the Official Journal).
(3) OJ No C 14, 20. 1. 1992, p. 11.
(4) OJ No L 330, 29. 11. 1990, p. 50.
(5) OJ No L 63, 13. 3. 1979, p. 1. Directive as last amended by the Second Directive 90/619/EEC (OJ No L 330, 29. 11. 1990, p. 50).
(6) OJ No L 374, 31. 12. 1991, p. 7.

and sufficient to achieve the mutual recognition of authorizations and prudential control systems, thereby making it possible to grant a single authorization valid throughout the Community and apply the principle of supervision by the home Member State;

6. Whereas, as a result, the taking up and the pursuit of the business of assurance are henceforth to be subject to the grant of a single official authorization issued by the competent authorities of the Member State in which an assurance undertaking has its head office; whereas such authorization enables an undertaking to carry on business throughout the Community, under the right of establishment or the freedom to provide services; whereas the Member State of the branch or of the provision of services may no longer require assurance undertakings which wish to carry on assurance business there and which have already been authorized in their home Member State to seek fresh authorization; whereas Directives 79/267/EEC and 90/619/EEC should therefore be amended along those lines;

7. Whereas the competent authorities of home Member States will henceforth be responsible for monitoring the financial health of assurance undertakings, including their state of solvency, the establishment of adequate technical provisions and the covering of those provisions by matching assets;

8. Whereas the performance of the operations referred to in Article 1 (2) (c) of Directive 79/267/EEC cannot under any circumstances affect the powers conferred on the respective authorities with regard to the entities holding the assets with which that provision is concerned;

9. Whereas certain provisions of this Directive define minimum standards; whereas a home Member State may lay down stricter rules for assurance undertakings authorized by its own competent authorities;

10. Whereas the competent authorities of the Member States must have at their disposal such means of supervision as are necessary to ensure the orderly pursuit of business by assurance undertakings throughout the Community whether carried on under the right of establishment or the freedom to provide services; whereas, in particular, they must be able to introduce appropriate safeguards or impose sanctions aimed at preventing irregularities and infringements of the provisions on assurance supervision;

11. Whereas the provisions on transfers of portfolios must be adapted to bring them into line with the single legal authorization system introduced by this Directive;

12. Whereas provision should be made for the specialization rule laid down by Directive 79/267/EEC to be relaxed so that those Member States which so wish are able to grant the same undertaking authorizations for the classes referred to in the Annex to Directive 79/267/EEC and the insurance business coming under classes 1 and 2 in the Annex to Directive 73/239/EEC [1]; whereas that possibility may, however, be subject to certain conditions as regards compliance with accounting rules and rules on winding-up;

13. Whereas it is necessary from the point of view of the protection of lives assured that every assurance undertaking should establish adequate technical provisions; whereas the calculation of such provisions is based for the most part on actuarial principles; whereas those principles should be coordinated in order to facilitate mutual recognition of the prudential rules applicable in the various Member States;

14. Whereas it is desirable, in the interests of prudence, to establish a minimum of coordination of rules limiting the rate of interest used in calculating the technical provisions; whereas, for the purposes of such limitation, since existing methods are all equally correct, prudential and equivalent, it seems appropriate to leave Member States a free choice as to the method to be used;

15. Whereas the rules governing the spread, localization and matching of the assets used to cover technical provisions must be coordinated in order to facilitate the mutual recognition of Member States' rules; whereas that coordination must take account of the measures on the liberalization of capital movements provided for in Council Directive 88/361/EEC of 24 June 1988 for the implementation of Article 67 of the Treaty [2] and the progress made by the Community towards economic and monetary union;

16. Whereas, however, the home Member State may not require assurance undertakings to invest the assets covering their technical provisions in particular

(1) First Council Directive 73/239/EEC of 24 July 1973 on the coordination of laws, regulations and administrative provisions relating to the taking-up and pursuit of the business of direct insurance other than life assurance (OJ No L 228, 16. 8. 1973, p. 3). Directive as last amended by Directive 90/618/EEC (OJ No L 330, 29. 11. 1990, p. 44).

(2) OJ No L 178, 8. 7. 1988, p. 5.

categories of assets, as such a requirement would be incompatible with the measures on the liberalization of capital movements provided for in Directive 88/361/EEC;

17. Whereas, pending the adoption of a directive on investment services harmonizing *inter alia* the definition of the concept of a regulated market, for the purposes of this Directive and without prejudice to such future harmonization that concept must be defined provisionally, to be replaced by the definition harmonized at Community level, which will give the home Member State of the market the responsibilities for these matters which this Directive transitionally gives to the assurance undertaking's home Member State;

18. Whereas the list of items of which the solvency margin required by Directive 79/267/EEC may be made up must be supplemented to take account of new financial instruments and of the facilities granted to other financial institutions for the constitution of their own funds;

19. Whereas the harmonization of assurance contract law is not a prior condition for the achievement of the internal market in assurance; whereas, therefore, the oppportunity afforded to the Member States of imposing the application of their law to assurance contracts covering commitments within their territories is likely to provide adequate safeguards for policy-holders;

20. Whereas within the framework of an internal market it is in the policy-holder's interest that he should have access to the widest possible range of assurance products available in the Community so that he can choose that which is best suited to his needs; whereas it is for the Member State of the commitment to ensure that there is nothing to prevent the marketing within its territory of all the assurance products offered for sale in the Community as long as they do not conflict with the legal provisions protecting the general good in force in the Member State of the commitment and in so far as the general good is not safeguarded by the rules of the home Member State, provided that such provisions must be applied without discrimination to all undertakings operating in that Member State and be objectively necessary and in proportion to the objective pursued;

21. Whereas the Member States must be able to ensure that the assurance products and contract documents used, under the right of establishment or the freedom to provide services, to cover commitments within their territories comply with such specific legal provisions protecting the general good as are applicable; whereas the systems of supervision to be employed must meet the requirements of an internal market but their employment may not constitute a prior condition for carrying on assurance business; whereas, from this standpoint, systems for the prior approval of policy conditions do not appear to be justified; whereas it is therefore necessary to provide for other systems better suited to the requirements of an internal market which enable every Member State to guarantee policy-holders adequate protection;

22. Whereas, for the purposes of implementing actuarial principles in conformity with this Directive, the home Member State may nevertheless require systematic notification of the technical bases used for calculating scales of premiums and technical provisions, with such notification of technical bases excluding notification of the general and special policy conditions and the undertaking's commercial rates;

23. Whereas in a single assurance market the consumer will have a wider and more varied choice of contracts; whereas, if he is to profit fully from this diversity and from increased competition, he must be provided with whatever information is necessary to enable him to choose the contract best suited to his needs; whereas this information requirement is all the more important as the duration of commitments can be very long; whereas the minimum provisions must therefore be coordinated in order for the consumer to receive clear and accurate information on the essential characteristics of the products proposed to him as well as the particulars of the bodies to which any complaints of policy-holders, assured persons or beneficiaries of contracts may be addressed;

24. Whereas publicity for assurance products is an essential means of enabling assurance business to be carried on effectively within the Community; whereas it is necessary to leave open to assurance undertakings the use of all normal means of advertising in the Member State of the branch or of provision of services; whereas Member States may nevertheless require compliance with their national rules on the form and content of advertising, whether laïd down pursuant to Community legislation on advertising or adopted by Member States for reasons of the general good;

25. Whereas, within the framework of the internal market, no Member State may continue to prohibit the simultaneous carrying on of assurance business within its territory under the right of establishment

and the freedom to provide services; whereas the option granted to Member States in this connection by Directive 90/619/EEC should therefore be abolished;

26. Whereas provision should be made for a system of penalties to be imposed when, in the Member State in which the commitment is entered into, an assurance undertaking does not comply with those provisions protecting the general good that are applicable to it;

27. Whereas some Member States do not subject assurance transactions to any form of indirect taxation, while the majority apply special taxes and other forms of contribution; whereas the structures and rates of such taxes and contributions vary considerably between the Member States in which they are applied; whereas it is desirable to prevent existing differences leading to distortions of competition in assurance services between Member States; whereas, pending subsequent harmonization, application of the tax systems and other forms of contribution provided for by the Member States in which commitments entered into are likely to remedy that problem and it is for the Member States to make arrangements to ensure that such taxes and contributions are collected;

28. Whereas it is important to introduce Community coordination on the winding-up of assurance undertakings; whereas it is henceforth essential to provide, in the event of the winding-up of an assurance undertaking, that the system of protection in place in each Member State must guarantee equality of treatment for all assurance creditors, irrespective of nationality and of the method of entering into the commitment;

29. Whereas technical adjustments to the detailed rules laid down in this Directive may be necessary from time to time to take account of the future development of the assurance industry; whereas the Commission will make such adjustments as and when necessary, after consulting the Insurance Committee set up by Directive 91/675/EEC (1), in the exercise of the implementing powers conferred on it by the Treaty;

30. Whereas it is necessary to adopt specific provisions intended to ensure smooth transition from the legal arrangements in existence when this Directive becomes applicable to those that it introduces; whereas care should be taken in such provisions not to place an additional workload on Member States' competent authorities;

(1) OJ No L 374, 31. 12. 1991, p. 32.

31. Whereas, pursuant to Article 8c of the Treaty, account should be taken of the extent of the effort which must be made by certain economies at different stages of development; whereas, therefore, transitional arrangements should be adopted for the gradual application of this Directive by certain Member States,

HAS ADOPTED THIS DIRECTIVE:

TITLE I

DEFINITIONS AND SCOPE

Article 1

For the purposes of this Directive:

(a) *assurance undertaking* shall mean an undertaking which has received official authorization in accordance with Article 6 of Directive 79/267/EEC;

(b) *branch* shall mean an agency or branch of an assurance undertaking, having regard to Article 3 of Directive 90/619/EEC;

(c) *commitment* shall mean a commitment represented by one of the kinds of insurance or operations referred to in Article 1 of Directive 79/267/EEC;

(d) *home Member State* shall mean the Member State in which the head office of the assurance undertaking covering the commitment is situated;

(e) *Member State of the branch* shall mean the Member State in which the branch covering the commitment is situated;

(f) *Member State of the provision of services* shall mean the Member State of the commitment, as defined in Article 2 (e) of Directive 90/619/EEC, if the commitment is covered by an assurance undertaking or a branch situated in another Member State;

(g) *control* shall mean the relationship between a parent undertaking and a subsidiary, as defined in Article 1 of Directive 83/349/EEC (1), or a similar relationship between any natural or legal person and an undertaking;

(1) Seventh Council Directive 83/349/EEC of 13 June 1983 based on Article 54 (3) (g) of the Treaty on consolidated accounts (OJ No L 193, 18. 7. 1983, p. 1). Directive as last amended by Directive 90/605/EEC (OJ No L 317, 16. 11. 1990, p. 60).

(h) *qualifying holding* shall mean a direct or indirect holding in an undertaking which represents 10% or more of the capital or of the voting rights or which makes it possible to exercise a significant influence over the management of the undertaking in which a holding subsists.

For the purposes of this definition, in the context of Articles 7 and 14 and of the other levels of holding referred to in Article 14, the voting rights referred to in Article 7 of Directive 88/627/EEC (1) shall be taken into consideration;

(i) *parent undertaking* shall mean a parent undertaking as defined in Articles 1 and 2 of Directive 83/349/EEC;

(j) *subsidiary* shall mean a subsidiary undertaking as defined in Articles 1 and 2 of Directive 83/349/EEC; any subsidiary of a subsidiary undertaking shall also be regarded as a subsidiary of the undertaking which is those undertakings' ultimate parent undertaking;

(k) *regulated market* shall mean a financial market regarded by an undertaking's home Member State as a regulated market pending the adoption of a definition in a Directive on investment services and characterized by:

— regular operation, and

— the fact that regulations issued or approved by the appropriate authorities define the conditions for the operation of the market, the conditions for access to the market and, where Council Directive 79/279/EEC of 5 March 1979 coordinating the conditions for the admission of securities to official stock-exchange listing (2) applies, the conditions for admission to listing imposed in that Directive or, where that Directive does not apply, the conditions to be satisfied by a financial instrument in order to be effectively dealt in on the market.

For the purposes of this Directive, a regulated market may be situated in a Member State or in a third country. In the latter event, the market must be recognized by the undertaking's home Member State and meet comparable requirements. Any financial instruments dealt in must be of a quality comparable to that of the instruments dealt in on the regulated market or markets of the Member State in question;

(l) *competent authorities* shall mean the national authorities which are empowered by law or regulation to supervise assurance undertakings.

Article 2

1. This Directive shall apply to the commitments and undertakings referred to in Article 1 of Directive 79/267/EEC.

2. In Article 1 (2) of Directive 79/267/EEC the words 'and are authorized in the country concerned' shall be deleted.

3. This Directive shall apply neither to classes of insurance or operations nor to undertakings or institutions to which Directive 79/267/EEC does not apply, nor shall it apply to the bodies referred to in Article 4 of that Directive.

TITLE II

THE TAKING-UP OF THE BUSINESS OF LIFE ASSURANCE

Article 3

Article 6 of Directive 79/267/EEC shall be replaced by the following:

'*Article 6*

The taking-up of the activities covered by this Directive shall be subject to prior official authorization.

Such authorization shall be sought from the authorities of the home Member State by:

(a) any undertaking which establishes its head office in the territory of that State;

(b) any undertaking which, having received the authorization required in the first subparagraph, extends its business to an entire class or to other classes.'

Article 4

Article 7 of Directive 79/267/EEC shall be replaced by the following:

'*Article 7*

1. Authorization shall be valid for the entire Community. It shall permit an undertaking to carry on business there, under either the right of establishment or freedom to provide services.

(1) Council Directive 88/627/EEC of 12 December 1988 on the information to be published when a major holding in a listed company is acquired or disposed of (OJ No L 348, 17. 12. 1988, p. 62).

(2) OJ No L 66, 13. 3. 1979, p. 21. Directive as last amended by Directive 82/148/EEC (OJ No L 62, 5. 3. 1982, p. 22).

2. Authorization shall be granted for a particular class of assurance as listed in the Annex. It shall cover the entire class, unless the applicant wishes to cover only some of the risks pertaining to that class.

The competent authorities may restrict authorization requested for one of the classes to the operations set out in the scheme of operations referred to in Article 9.

Each Member State may grant authorization for two or more of the classes, where its national laws permit such classes to be carried on simultaneously.'

Article 5

Article 8 of Directive 79/267/EEC shall be replaced by the following:

'Article 8

1. The home Member State shall require every assurance undertaking for which authorization is sought to:

(a) adopt one of the following forms:

— in the case of the Kingdom of Belgium: "société anonyme/naamloze vennootschap", "société en commandite par actions/commanditaire vennootschap op aandelen", "association d'assurance mutuelle/onderlinge verzekeringsvereniging", "société coopérative/coöperatieve vennootschap",

— in the case of the Kingdom of Denmark: "aktieselskaber", "gensidige selskaber", "pensionskasser omfattet af lov om forsikringsvirksomhed (tværgående pensionskasser)",

— in the case of the Federal Republic of Germany: "Aktiengesellschaft", "Versicherungsverein auf Gegenseitigkeit", "öffentlich-rechtliches Wettbewerbsversicherungsunternehmen",

— in the case of the French Republic: "société anonyme", "société d'assurance mutuelle", "institution de prévoyance régie par le code de la sécurité sociale", "institution de prévoyance régie par le code rural" and "mutuelles régies par le code de la mutualité",

— in the case of Ireland: incorporated companies limited by shares or by guarantee or unlimited, societies registered under the Industrial and Provident Societies Acts and societies registered under the Friendly Societies Acts,

— in the case of the Italian Republic: "società per azioni", "società cooperativa", "mutua di assicurazione",

— in the case of the Grand Duchy of Luxembourg: "société anonyme", "société en commandite par actions", "association d'assurances mutuelles", "société coopérative",

— in the case of the Kingdom of the Netherlands: "naamloze vennootschap", "onderlinge waarborgmaatschappij",

— in the case of the United Kingdom: incorporated companies limited by shares or by guarantee or unlimited, societies registered under the Industrial and Provident Societies Acts, societies registered or incorporated under the Friendly Societies Acts, the association of underwriters known as Lloyd's,

— in the case of the Hellenic Republic: "ανώνυμη εταιρία",

— in the case of the Kingdom of Spain: "sociedad anonima", "sociedad mutua", "sociedad cooperativa",

— in the case of the Portuguese Republic: "sociedade anónima", "mútua de seguros".

An assurance undertaking may also adopt the form of a European company when that has been established.

Furthermore, Member States may, where appropriate, set up undertakings in any public-law form provided that such bodies have as their object insurance operations under conditions equivalent to those under which private-law undertakings operate;

(b) limit its objects to the business provided for in this Directive and operations directly arising therefrom, to the exclusion of all other commercial business;

(c) submit a scheme of operations in accordance with Article 9;

(d) possess the minimum guarantee fund provided for in Article 20 (2);

(e) be effectively run by persons of good repute with appropriate professional qualifications or experience.

2. An undertaking seeking authorization to extend its business to other classes or to extend an authorization covering only some of the risks pertaining to one class shall be required to submit a scheme of operations in accordance with Article 9.

It shall, furthermore, be required to show proof that it possesses the solvency margin provided for in Article 19 and the guarantee fund referred to in Article 20 (1) and (2).

3. Member States shall not adopt provisions requiring the prior approval or systematic notification of general and special policy conditions, of scales of premiums, of the technical bases, used in particular for calculating scales of premiums and technical provisions or of forms and other printed documents which an assurance undertaking intends to use in its dealings with policy-holders.

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Member State carries on business through a branch, the competent authorities of the home Member State may, after having first informed the competent authorities of the Member State of the branch, carry out themselves, or through the intermediary of persons they appoint for that purpose, on-the-spot verification of the information necessary to ensure the financial supervision of the undertaking. The authorities of the Member State of the branch may participate in that verification'.

Article 10

Article 23 (2) and (3) of Directive 79/267/EEC shall be replaced by the following:

'2. Member States shall require assurance undertakings with head offices within their territories to render periodically the returns, together with statistical documents, which are necessary for the purposes of supervision. The competent authorities shall provide each other with any documents and information that are useful for the purposes of supervision.

3. Every Member State shall take all steps necessary to ensure that the competent authorities have the powers and means necessary for the supervision of the business of assurance undertakings with head offices within their territories, including business carried on outside those territories, in accordance with the Council directives governing those activities and for the purpose of seeing that they are implemented.

These powers and means must, in particular, enable the competent authorities to:

(a) make detailed enquiries regarding the undertaking's situation and the whole of its business, *inter alia* by:

— gathering information or requiring the submission of documents concerning its assurance business,

— carrying out on-the-spot investigations at the undertaking's premises;

(b) take any measures, with regard to the undertaking, its directors or managers or the persons who control it, that are appropriate and necessary to ensure that the undertaking's business continues to comply with the laws, regulations and administrative provisions with which the undertaking must comply in each Member State and in particular with the scheme of operations in so far as it remains mandatory, and to prevent or remedy any irregularities prejudicial to the interests of the assured persons;

(c) ensure that those measures are carried out, if need be by enforcement, where appropriate through judicial channels.

Member States may also make provision for the competent authorities to obtain any information regarding contracts which are held by intermediaries.'

Article 11

1. Article 6 (2) to (7) of Directive 90/619/EEC shall be deleted.

2. Under the conditions laid down by national law, each Member State shall authorize assurance undertakings with head offices within its territory to transfer all or part of their portfolios of contracts, concluded under either the right of establishment or the freedom to provide services, to an accepting office established within the Community, if the competent authorities of the home Member State of the accepting office certify that after taking the transfer into account the latter possesses the necessary solvency margin.

3. Where a branch proposes to transfer all or part of its portfolio of contracts, concluded under either the right of establishment or the freedom to provide services, the Member State of the branch shall be consulted.

4. In the circumstances referred to in paragraph 2 and 3, the authorities of the home Member State of the transferring undertaking shall authorize the transfer after obtaining the agreement of the competent authorities of the Member States of the commitment.

5. The competent authorities of the Member States consulted shall give their opinion or consent to the competent authorities of the home Member State of the transferring assurance undertaking within three months of receiving a request; the absence of any response within that period from the authorities consulted shall be considered equivalent to a favourable opinion or tacit consent.

6. A transfer authorized in accordance with this Article shall be published as laid down by national law in the Member State of the commitment. Such transfers shall automatically be valid against policy-holders, the assured persons and any other person having rights or obligations arising out of the contracts transferred.

This provision shall not affect the Member States' rights to give policy-holders the option of cancelling contracts within a fixed period after a transfer.

Article 12

1. Article 24 of Directive 79/267/EEC shall be replaced by the following:

'Article 24

1. If an undertaking does not comply with Article 17, the competent authority of its home Member State may prohibit the free disposal of its

assets after having communicated its intention to the competent authorities of the Member States of commitment.

2. For the purposes of restoring the financial situation of an undertaking the solvency margin of which has fallen below the minimum required under Article 19, the competent authority of the home Member State shall require that a plan for the restoration of a sound financial position be submitted for its approval.

In exceptional circumstances, if the competent authority is of the opinion that the financial situation of the undertaking will further deteriorate, it may also restrict or prohibit the free disposal of the undertaking's assets. It shall inform the authorities of other Member States within the territories of which the undertaking carries on business of any measures it has taken and the latter shall, at the request of the former, take the same measures.

3. If the solvency margin falls below the guarantee fund as defined in Article 20, the competent authority of the home Member State shall require the undertaking to submit a short-term finance scheme for its approval.

It may also restrict or prohibit the free disposal of the undertaking's assets. It shall inform the authorities of other Member States within the territories of which the undertaking carries on business accordingly and the latter shall, at the request of the former, take the same measures.

4. The competent authorities may further take all measures necessary to safeguard the interests of the assured persons in the cases provided for in paragraphs 1, 2 and 3.

5. Each Member State shall take the measures necessary to be able in accordance with its national law to prohibit the free disposal of assets located within its territory at the request, in the cases provided for in paragraphs 1, 2 and 3, of the undertaking's home Member State, which shall designate the assets to be covered by such measures.'

Article 13

Article 26 of Directive 79/267/EEC shall be replaced by the following:

'*Article 26*

1. Authorization granted to an assurance undertaking by the competent authority of its home Member State may be withdrawn by that authority if that undertaking:

(a) does not make use of the authorization within 12 months, expressly renounces it or ceases to carry on business for more than six months, unless the Member State concerned has made provision for authorization to lapse in such cases;

(b) no longer fulfils the conditions for admission;

(c) has been unable, within the time allowed, to take the measures specified in the restoration plan or finance scheme referred to in Article 24;

(d) fails seriously in its obligations under the regulations to which it is subject.

In the event of the withdrawal or lapse of the authorization, the competent authority of the home Member State shall notify the competent authorities of the other Member States accordingly and they shall take appropriate measures to prevent the undertaking from commencing new operations within their territories, under either the freedom of establishment or the freedom to provide services. The home Member State's competent authority shall, in conjunction with those authorities, take all necessary measures to safeguard the interests of the assured persons and shall restrict, in particular, the free disposal of the assets of the undertaking in accordance with Article 24 (1), (2), second subparagraph, or (3), second subparagraph.

2. Any decision to withdraw an authorization shall be supported by precise reasons and notified to the undertaking in question.'

Article 14

1. Member States shall require any natural or legal person who proposes to acquire, directly or indirectly, a qualifying holding in an assurance undertaking first to inform the competent authorities of the home Member State, indicating the size of the intended holding. Such a person must likewise inform the competent authorities of the home Member State if he proposes to increase his qualifying holding so that the proportion of the voting rights or of the capital held by him would reach or exceed 20, 33 or 50% or so that the assurance undertaking would become his subsidiary.

The competent authorities of the home Member State shall have a maximum of three months from the date of the notification provided for in the first subparagraph to oppose such a plan if, in view of the need to ensure sound and prudent management of the assurance undertaking, they are not satisfied as to the qualifications of the person referred to in the first subparagraph. If they do not oppose the plan in question they may fix a maximum period for its implementation.

2. Member States shall require any natural or legal person who proposes to dispose, directly or indirectly, of a qualifying holding in an assurance undertaking first to

inform the competent authorities of the home Member State, indicating the size of his intended holding. Such a person must likewise inform the competent authorities if he proposes to reduce his qualifying holding so that the proportion of the voting rights or of the capital held by him would fall below 20, 33 or 50% or so that the assurance undertaking would cease to be his subsidiary.

3. On becoming aware of them, assurance undertakings shall inform the competent authorities of their home Member States of any acquisitions or disposals of holdings in their capital that cause holdings to exceed or fall below one of the thresholds referred to in paragraphs 1 and 2.

They shall also, at least once a year, inform them of the names of shareholders and members possessing qualifying holdings and the sizes of such holdings as shown, for example, by the information received at the annual general meetings of shareholders and members or as a result of compliance with the regulations relating to companies listed on stock exchanges.

4. Member States shall require that, if the influence exercised by the persons referred to in paragraph 1 is likely to operate to the detriment of the prudent and sound management of the assurance undertaking, the competent authorities of the home Member State shall take appropriate measures to put an end to that situation. Such measures may consist, for example, in injunctions, sanctions against directors and managers, or the suspension of the exercise of the voting rights attaching to the shares held by the shareholders or members in question.

Similar measures shall apply to natural or legal persons failing to comply with the obligation to provide prior information, as laid down in paragraph 1. If a holding is acquired despite the opposition of the competent authorities, the Member States shall, regardless of any other sanctions to be adopted, provide either for exercise of the corresponding voting rights to be suspended, or for the nullity of votes cast or for the possibility of their annulment.

Article 15

1. The Member States shall provide that all persons working or who have worked for the competent authorities, as well as auditors or experts acting on behalf of the competent authorities, shall be bound by the obligation of professional secrecy. This means that no confidential information which they may receive in the course of their duties may be divulged to any person or authority whatsoever, except in summary or aggregate form, such that individual assurance undertakings cannot be identified, without prejudice to cases covered by criminal law.

Nevertheless, where an assurance undertaking has been declared bankrupt or is being compulsorily wound up, confidential information which does not concern third parties involved in attempts to rescue that undertaking may be divulged in civil or commercial proceedings.

2. Paragraph 1 shall not prevent the competent authorities of the different Member States from exchanging information in accordance with the directives applicable to assurance undertakings. That information shall be subject to the conditions of professional secrecy indicated in paragraph 1.

3. Member States may conclude cooperation agreements, providing for exchanges of information, with the competent authorities of third countries only if the information disclosed is subject to guarantees of professional secrecy at least equivalent to those referred to in this Article.

4. Competent authorities receiving confidential information under paragraphs 1 or 2 may use it only in the course of their duties:

— to check that the conditions governing the taking-up of the business of assurance are met and to facilitate monitoring of the conduct of such business, especially with regard to the monitoring of technical provisions, solvency margins, administrative and accounting procedures and internal control mechanisms, or

— to impose sanctions, or

— in administrative appeals against decisions of the competent authority, or

— in court proceedings initiated pursuant to Article 50 or under special provisions provided for in the directives adopted in the field of assurance undertakings.

5. Paragraphs 1 and 4 shall not preclude the exchange of information within a Member State, where there are two or more competent authorities in the same Member State, or, between Member States, between competent authorities and:

— authorities responsible for the official supervision of credit institutions and other financial organizations and the authorities responsible for the supervision of financial markets,

— bodies involved in the liquidation and bankruptcy of assurance undertakings and in other similar procedures, and

— persons responsible for carrying out statutory audits of the accounts of assurance undertakings and other financial institutions,

in the discharge of their supervisory functions, and the disclosure, to bodies which administer (compulsory) winding-up proceedings or guarantee funds, of information necessary to the performance of their duties. The information received by these authorities, bodies and persons shall be subject to the obligation of professional secrecy laid down in paragraph 1.

6. In addition, notwithstanding paragraphs 1 and 4, Member States may, under provisions laid down by law, authorize the disclosure of certain information to other departments of their central government administrations responsible for legislation on the supervision of credit institutions, financial institutions, investment services and assurance undertakings and to inspectors acting on behalf of those departments.

However, such disclosures may be made only where necessary for reasons of prudential control.

However, Member States shall provide that information received under paragraphs 2 and 5 and that obtained by means of the on-the-spot verification referred to in Article 16 of Directive 79/267/EEC may never be disclosed in the cases referred to in this paragraph except with the express consent of the competent authorities which disclosed the information or of the competent authorities of the Member State in which on-the-spot verification was carried out.

Article 16

Article 13 of Directive 79/267/EEC shall be replaced by the following:

'Article 13

1. Without prejudice to paragraphs 3 and 7, no undertaking may be authorized both pursuant to this Directive and pursuant to Directive 73/239/EEC.

2. However, Member States may provide that:

— undertakings authorized pursuant to this Directive may also obtain authorization, in accordance with Article 6 of Directive 73/239/EEC for the risks listed in classes 1 and 2 in the Annex to that Directive,

— undertakings authorized pursuant to Article 6 of Directive 73/239/EEC solely for the risks listed in classes 1 and 2 in the Annex to that Directive may obtain authorization pursuant to this Directive.

3. Subject to paragraph 6, undertakings referred to in paragraph 2 and those which at the time of notification of this Directive carry on simultaneously both of the activities covered by this Directive and by Directive 73/239/EEC may continue to do so, provided that each activity is separately managed in accordance with Article 14.

4. Member States may provide that the undertakings referred to in paragraph 2 shall comply with the accounting rules governing undertakings authorized pursuant to this Directive for all of their activities. Pending coordination in this respect, Member States may also provide that, with regard to rules on winding-up, activities relating to the risks listed in classes 1 and 2 in the Annex to Directive 73/239/EEC carried on by the undertakings referred to in paragraph 2 shall be governed by the rules applicable to life assurance activities.

5. Where an undertaking carrying on the activities referred to in the Annex to Directive 73/239/EEC has financial, commercial or administrative links with an undertaking carrying on the activities covered by this Directive, the supervisory authorities of the Member States within whose territories the head offices of those undertakings are situated shall ensure that the accounts of the undertakings in question are not distorted by agreements between these undertakings or by any arrangement which could affect the apportionment of expenses and income.

6. Any Member State may require undertakings whose head offices are situated in its territory to cease, within a period to be determined by the Member State concerned, the simultaneous pursuit of activities in which they were engaged at the time of notification of this Directive.

7. The provisions of this Article shall be reviewed on the basis of a report from the Commission to the Council in the light of future harmonization of the rules on winding-up, and in any case before 31 December 1999.'

Article 17

Article 35 of Directive 79/267/EEC and Article 18 of Directive 90/619/EEC shall be deleted.

Chapter 2

Article 18

Article 17 of Directive 79/267/EEC shall be replaced by the following:

'Article 17

1. The home Member State shall require every assurance undertaking to establish sufficient technical

provisions, including mathematical provisions, in respect of its entire business.

The amount of such technical provisions shall be determined according to the following principles:

A. (i) The amount of the technical life-assurance provisions shall be calculated by a sufficiently prudent prospective actuarial valuation, taking account of all future liabilities as determined by the policy conditions for each existing contract, including:

— all guaranteed benefits, including guaranteed surrender values,

— bonuses to which policy-holders are already either collectively or individually entitled, however those bonuses are described — vested, declared or allotted,

— all options available to the policy-holder under the terms of the contract,

— expenses, including commissions;

taking credit for future premiums due;

(ii) the use of a retrospective method is allowed, if it can be shown that the resulting technical provisions are not lower than would be required under a sufficiently prudent prospective calculation or if a prospective method cannot be used for the type of contract involved;

(iii) a prudent valuation is not a "best estimate" valuation, but shall include an appropriate margin for adverse deviation of the relevant factors;

(iv) the method of valuation for the technical provisions must not only be prudent in itself, but must also be so having regard to the method of valuation for the assets covering those provisions;

(v) technical provisions shall be calculated separately for each contract. The use of appropriate approximations or generalizations is allowed, however, where they are likely to give approximately the same result as individual calculations. The principle of separate calculation shall in no way prevent the establishment of additional provisions for general risks which are not individualized;

(vi) where the surrender value of a contract is guaranteed, the amount of the mathematical provisions for the contract at any time shall be at least as great as the value guaranteed at that time.

B. The rate of interest used shall be chosen prudently. It shall be determined in accordance with the rules of the competent authority in the home Member State, applying the following principles:

(a) for all contracts, the competent authority of the undertaking's home Member State shall fix one or more maximum rates of interest, in particular in accordance with the following rules:

(i) when contracts contain an interest rate guarantee, the competent authority in the home Member State shall set a single maximum rate of interest. It may differ according to the currency in which the contract is denominated, provided that it is not more than 60% of the rate on bond issues by the State in whose currency the contract is denominated. In the case of a contract denominated in ecus, this limit shall be set by reference to ecu-denominated issues by the Community institutions.

If a Member State decides, pursuant to the second sentence of the preceding paragraph, to set a maximum rate of interest for contracts denominated in another Member State's currency, it shall first consult the competent authority of the Member State in whose currency the contract is denominated;

(ii) however, when the assets of the undertaking are not valued at their purchase price, a Member State may stipulate that one or more maximum rates may be calculated taking into account the yield on the corresponding assets currently held, minus a prudential margin and, in particular for contracts with periodic premiums, furthermore taking into account the anticipated yield on future assets. The prudential margin and the maximum rate or rates of interest applied to the anticipated yield on future assets shall be fixed by the competent authority of the home Member State;

(b) the establishment of a maximum rate of interest shall not imply that the undertaking is bound to use a rate as high as that;

(c) the home Member State may decide not to apply (a) to the following categories of contracts:

— unit-linked contracts,

— single-premium contracts for a period of up to eight years,

— without-profits contracts, and annuity contracts with no surrender value.

In the cases referred to in the last two indents of the first subparagraph, in choosing a prudent rate of interest, account may be taken of the currency in which the contract is denominated and corresponding assets currently held and where the undertaking's assets are valued at their current value, the anticipated yield on future assets.

Under no circumstances may the rate of interest used be higher than the yield on assets as calculated in accordance with the accounting rules in the home Member State, less an appropriate deduction;

(d) the Member State shall require an undertaking to set aside in its accounts a provision to meet interest-rate commitments *vis-à-vis* policy-holders if the present or foreseeable yield on the undertaking's assets is insufficient to cover those commitments;

(e) the Commission and the competent authorities of the Member States which so request shall be notified of the maximum rates of interest set under (a).

C. The statistical elements of the valuation and the allowance for expenses used shall be chosen prudently, having regard to the State of the commitment, the type of policy and the administrative costs and commissions expected to be incurred.

D. In the case of participating contracts, the method of calculation for technical provisions may take into account, either implicitly or explicitly, future bonuses of all kinds, in a manner consistent with the other assumptions on future experience and with the current method of distribution of bonuses.

E. Allowance for future expenses may be made implicitly, for instance by the use of future premiums net of management charges. However, the overall allowance, implicit or explicit, shall be not less than a prudent estimate of the relevant future expenses.

F. The method of calculation of technical provisions shall not be subject to discontinuities from year to year arising from arbitrary changes to the method or the bases of calculation and shall be such as to recognize the distribution of profits in an appropriate way over the duration of each policy.

2. Assurance undertakings shall make available to the public the bases and methods used in the calculation of the technical provisions, including provisions for bonuses.

3. The home Member State shall require every assurance undertaking to cover the technical provisions in respect of its entire business by matching assets, in accordance with Article 24 of Directive 92/96/EEC. In respect of business written in the Community, these assets must be localized within the Community. Member States shall not require assurance undertakings to localize their assets in a particular Member State. The home Member State may, however, permit relaxations in the rules on the localization of assets.

4. If the home Member State allows any technical provisions to be covered by claims against reassurers, it shall fix the percentage so allowed. In such case, it may not require the localization of the assets representing such claims.'

Article 19

Premiums for new business shall be sufficient, on reasonable actuarial assumptions, to enable assurance undertakings to meet all their commitments and, in particular, to establish adequate technical provisions.

For this purpose, all aspects of the financial situation of an assurance undertaking may be taken into account, without the input from resources other than premiums and income earned thereon being systematic and permanent in such a way that it may jeopardize the undertaking's solvency in the long term.

Article 20

The assets covering the technical provisions shall take account of the type of business carried on by an undertaking in such a way as to secure the safety, yield and marketability of its investments, which the undertaking shall ensure are diversified and adequately spread.

Article 21

1. The home Member State may not authorize assurance undertakings to cover their technical provisions with any but the following categories of assets:

A. *Investments*

(a) debt securities, bonds and other money- and capital-market instruments;

(b) loans;

(c) shares and other variable-yield participations;

(d) units in undertakings for collective investment in transferable securities and other investment funds;

(e) land, buildings and immovable property rights;

B. *Debts and claims*

(f) debts owed by reassurers, including reassurers' shares of technical provisions;

(g) deposits with and debts owed by ceding undertakings;

(h) debts owed by policy-holders and intermediaries arising out of direct and reassurance operations;

(i) advances against policies;

(j) tax recoveries;

(k) claims against guarantee funds;

C. *Others*

(l) tangible fixed assets, other than land and buildings, valued on the basis of prudent amortization;

(m) cash at bank and in hand, deposits with credit institutions and any other body authorized to receive deposits;

(n) deferred acquisition costs;

(o) accrued interest and rent, other accrued income and prepayments;

(p) reversionary interests.

In the case of the association of underwriters known as Lloyd's, asset categories shall also include guarantees and letters of credit issued by credit institutions within the meaning of Directive 77/780/EEC (1) or by assurance undertakings, together with verifiable sums arising out of life assurance policies, to the extent that they represent funds belonging to members.

The inclusion of any asset or category of assets listed in the first subparagraph shall not mean that all these assets should automatically be accepted as cover for technical provisions. The home Member State shall lay down more detailed rules fixing the conditions for the use of acceptable assets; in this connection, it may require valuable security or guarantees, particularly in the case of debts owed by reassurers.

In determining and applying the rules which it lays down, the home Member State shall, in particular, ensure that the following principles are complied with:

(i) assets covering technical provisions shall be valued net of any debts arising out of their acquisition;

(ii) all assets must be valued on a prudent basis, allowing for the risk of any amounts not being realizable. In particular, tangible fixed assets other than land and buildings may be accepted as cover for technical provisions only if they are valued on the basis of prudent amortization;

(iii) loans, whether to undertakings, to a State or international organization, to local or regional authorities or to natural persons, may be accepted as cover for technical provisions only if there are sufficient guarantees as to their security, whether these are based on the status of the borrower, mortgages, bank guarantees or guarantees granted by assurance undertakings or other forms of security;

(iv) derivative instruments such as options, futures and swaps in connection with assets covering technical provisions may be used in so far as they contribute to a reduction of investment risks or facilitate efficient portfolio management. They must be valued on a prudent basis and may be taken into account in the valuation of the underlying assets;

(v) transferrable securities which are not dealt in on a regulated market may be accepted as cover for technical provisions only if they can be realized in the short term or if they are holdings in credits institutions, in assurance undertakings, within the limits permitted by Article 8 of Directive 79/267/EEC, or in investment undertakings established in a Member State;

(vi) debts owed by and claims against a third party may be accepted as cover for the technical provisions only after deduction of all amounts owed to the same third party;

(1) First Council Directive 77/780/EEC of 12 December 1977 on the coordination of the laws, regulations and administrative provisions relating to the taking up and pursuit of the business of credit institutions (OJ No L 322, 17. 12. 1977, p. 30). Directive as last amended by Directive 89/646/EEC (OJ No L 386, 30. 12. 1989, p. 1).

(vii) the value of any debts and claims accepted as cover for technical provisions must be calculated on a prudent basis, with due allowance for the risk of any amounts not being realizable. In particular, debts owed by policy-holders and intermediaries arising out of assurance and reassurance operations may be accepted only in so far as they have been outstanding for not more than three months;

(viii) where the assets held include an investment in a subsidiary undertaking which manages all or part of the assurance undertaking's investments on its behalf, the home Member State must, when applying the rules and principles laid down in this Article, take into account the underlying assets held by the subsidiary undertaking; the home Member State may treat the assets of other subsidiaries in the same way;

(ix) deferred acquisition costs may be accepted as cover for technical provisions only to the extent that this is consistent with the calculation of the mathematical provisions.

2. Notwithstanding paragraph 1, in exceptional circumstances and at an assurance undertaking's request, the home Member State may, temporarily and under a properly reasoned decision, accept other categories of assets as cover for technical provisions, subject to Article 20.

Article 22

1. As regards the assets covering technical provisions, the home Member State shall require every assurance undertaking to invest no more than:

(a) 10% of its total gross technical provisions in any one piece of land or building, or a number of pieces of land or buildings close enough to each other to be considered effectively as one investment;

(b) 5% of its total gross technical provisions in shares and other negotiable securities treated as shares, bonds, debt securities and other money- and capital-market instruments from the same undertaking, or in loans granted to the same borrower, taken together, the loans being loans other than those granted to a State, regional or local authority or to an international organization of which one or more Member States are members. This limit may be raised to 10% if an undertaking invests not more than 40% of its gross technical provisions in the loans or securities of issuing bodies and borrowers in each of which it invests more than 5% of its assets;

(c) 5% of its total gross technical provisions in unsecured loans, including 1% for any single unsecured loan, other than loans granted to credit institutions, assurance undertakings — in so far as Article 8 of Directive 79/267/EEC allows it — and investment undertakings established in a Member State. The limits may be raised to 8 and 2% respectively by a decision taken on a case-by-case basis by the competent authority of the home Member State;

(d) 3% of its total gross technical provisions in the form of cash in hand;

(e) 10% of its total gross technical provisions in shares, other securities treated as shares and debt securities which are not dealt in on a regulated market.

2. The absence of a limit in paragraph 1 on investment in any particular category does not imply that assets in that category should be accepted as cover for technical provisions without limit. The home Member State shall lay down more detailed rules fixing the conditions for the use of acceptable assets. In particular it shall ensure, in the determination and the application of those rules, that the following principles are complied with:

(i) assets covering technical provisions must be diversified and spread in such a way as to ensure that there is no excessive reliance on any particular category of asset, investment market or investment;

(ii) investment in particular types of asset which show high levels of risk, whether because of the nature of the asset or the quality of the issuer, must be restricted to prudent levels;

(iii) limitations on particular categories of asset must take account of the treatment of reassurance in the calculation of technical provisions;

(iv) where the assets held include an investment in a subsidiary undertaking which manages all or part of the assurance undertaking's investments on its behalf, the home Member State must, when applying the rules and principles laid down in this Article, take into account the underlying assets held by the subsidiary undertaking; the home Member State may treat the assets of other subsidiaries in the same way;

(v) the percentage of assets covering technical provisions which are the subject of non-liquid investments must be kept to a prudent level;

(vi) where the assets held include loans to or debt securities issued by certain credit institutions, the home Member State may, when applying the rules and principles contained in this Article, take into account the underlying assets held by such credit institutions. This treatment may be applied only where the credit institution has its head office in a Member State, is entirely owned by that Member State and/or that State's local authorities and its business, according to its memorandum and articles of association, consists of extending, through its intermediaries, loans to, or guaranteed by, States or local authorities or of loans to bodies closely linked to the State or to local authorities.

3. In the context of the detailed rules laying down the conditions for the use of acceptable assets, the Member State shall give more limitative treatment to:

— any loan unaccompanied by a bank guarantee, a guarantee issued by an assurance undertaking, a mortgage or any other form of security, as compared with loans accompanied by such collateral,

— UCITS not coordinated within the meaning of Directive 85/611/EEC (1) and other investment funds, as compared with UCITS coordinated within the meaning of that Directive,

— securities which are not dealt in on a regulated market, as compared with those which are,

— bonds, debt securities and other money- and capital-market instruments not issued by States, local or regional authorities or undertakings belonging to Zone A as defined in Directive 89/647/EEC (2), or the issuers of which are international organizations not numbering at least one Community Member State among their members, as compared with the same financial instruments issued by such bodies.

4. Member States may raise the limit laid down in paragraph 1 (b) to 40% in the case of certain debt securities when these are issued by a credit institution which has its head office in a Member State and is subject by law to special official supervision designed to protect the holders of those debt securities. In particular, sums deriving from the issue of such debt securities must be invested in accordance with the law in assets which, during the whole period of validity of the debt securities, are capable of covering claims attaching to debt securities and which, in the event of failure of the issuer, would be used on a priority basis for the reimbursement of the principal and payment of the accrued interest.

5. Member States shall not require assurance undertakings to invest in particular categories of assets.

6. Notwithstanding paragraph 1, in exceptional circumstances and at the assurance undertaking's request, the home Member State may, temporarily and under a properly reasoned decision, allow exceptions to the rules laid down in paragraph 1 (a) to (e), subject to Article 20.

Article 23

1. Where the benefits provided by a contract are directly linked to the value of units in an UCITS or to the value of assets contained in an internal fund held by the insurance undertaking, usually divided into units, the technical provisions in respect of those benefits must be represented as closely as possible by those units or, in the case where units are not established, by those assets.

2. Where the benefits provided by a contract are directly linked to a share index or some other reference value other than those referred to in paragraph 1, the technical provisions in respect of those benefits must be represented as closely as possible either by the units deemed to represent the reference value or, in the case where units are not established, by assets of appropriate security and marketability which correspond as closely as possible with those on which the particular reference value is based.

3. Articles 20 and 22 shall not apply to assets held to match liabilities which are directly linked to the benefits referred to in paragraphs 1 and 2. References to the technical provisions in Article 22 shall be to the technical provisions excluding those in respect of such liabilities.

4. Where the benefits referred to in paragraph 1 and 2 include a guarantee of investment performance or some

(1) Council Directive 85/611/EEC of 20 December 1985 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) (OJ No L 375, 31. 12. 1985, p. 3). Directive as amended by Directive 88/220/EEC (OJ No L 100, 19. 4. 1988, p. 31).

(2) Council Directive 89/647/EEC of 18 December 1989 on a solvency ratio for credit institutions (OJ No L 386, 30. 12. 1989, p. 14).

other guaranteed benefit, the corresponding additional technical provisions shall be subject to Articles 20, 21 and 22.

Article 24

1. For the purposes of Articles 17 (3) and 28 of Directive 79/267/EEC, Member States shall comply with Annex I to this Directive as regards the matching rules.

2. This Article shall not apply to the commitments referred to in Article 23 of this Directive.

Article 25

Article 18, second subparagraph, point 1 of Directive 79/267/EEC shall be replaced by the following:

'1. the assets of the undertaking free of any foreseeable liabilities, less any intangible items. In particular the following shall be included:

— the paid-up share capital or, in the case of a mutual assurance undertaking, the effective initial fund plus any members' accounts which meet all the following criteria:

(a) the memorandum and articles of association must stipulate that payments may be made from these accounts to members only in so far as this does not cause the solvency margin to fall below the required level, or, after the dissolution of the undertaking, if all the undertaking's other debts have been settled;

(b) the memorandum and articles of association must stipulate, with respect to any such payments for reasons other than the individual termination of membership, that the competent authorities must be notified at least one month in advance and can prohibit the payment within that period;

(c) the relevant provisions of the memorandum and articles of association may be amended only after the competent authorities have declared that they have no objection to the amendment, without prejudice to the criteria stated in (a) and (b),

— one half of the unpaid share capital or initial fund, once the paid-up part amounts to 25% of that share capital or fund,

— reserves (statutory reserves and free reserves) not corresponding to underwriting liabilities,

— any profits brought forward,

— cumulative preferential share capital and subordinated loan capital may be included but, if so, only up to 50% of the margin, no more than 25% of which shall consist of subordinated loans with a fixed maturity, or fixed-term cumulative preferential share capital, if the following minimum criteria are met:

(a) in the event of the bankruptcy or liquidation of the assurance undertaking, binding agreements must exist under which the subordinated loan capital or preferential share capital ranks after the claims of all other creditors and is not to be repaid until all other debts outstanding at the time have been settled.

Subordinated loan capital must also fulfil the following conditions:

(b) only fully paid-up funds may be taken into account;

(c) for loans with a fixed maturity, the original maturity must be at least five years. No later than one year before the repayment date the assurance undertaking must submit to the competent authorities for their approval a plan showing how the solvency margin will be kept at or brought to the required level at maturity, unless the extent to which the loan may rank as a component of the solvency margin is gradually reduced during at least the last five years before the repayment date. The competent authorities may authorize the early repayment of such loans provided application is made by the issuing assurance undertaking and its solvency margin will not fall below the required level;

(d) loans the maturity of which is not fixed must be repayable only subject to five years' notice unless the loans are no longer considered as a component of the solvency margin or unless the prior consent of the competent authorities is specifically required for early repayment. In the latter event the assurance undertaking must notify the competent authorities at least six months before the date of the proposed repayment, specifying the actual and required solvency margin both before and after that repayment. The competent authorities shall authorize repayment only if the assurance undertaking's solvency margin will not fall below the required level;

(e) the loan agreement must not include any clause providing that in specified circumstances, other than the winding-up of the assurance undertaking, the debt will become repayable before the agreed repayment dates;

(f) the loan agreement may be amended only after the competent authorities have declared that they have no objection to the amendment,

— securities with no specified maturity date and other instruments that fulfil the following conditions, including cumulative preferential shares other than those mentioned in the preceding indent, up to 50 % of the margin for the total of such securities and the subordinated loan capital referred to in the preceding indent:

(a) they may not be repaid on the initiative of the bearer or without the prior consent of the competent authority;

(b) the contract of issue must enable the assurance undertaking to defer the payment of interest on the loan;

(c) the lender's claims on the assurance undertaking must rank entirely after those of all non-subordinated creditors;

(d) the documents governing the issue of the securities must provide for the loss-absorption capacity of the debt and unpaid interest, while enabling the assurance undertaking to continue its business;

(e) only fully paid-up amounts may be taken into account.'

Article 26

No more than three years after the date of application of this Directive, the Commission shall submit a report to the Insurance Committee on the need for further harmonization of the solvency margin.

Article 27

Article 21 of Directive 79/267/EEC shall be replaced by the following:

'*Article 21*

1. Member States shall not prescribe any rules as to the choice of the assets that need not be used as cover for the technical provisions referred to in Article 17.

2. Subject to Article 17 (3), Article 24 (1), (2), (3) and (5) and the second subparagraph of Article 26 (1), Member States shall not restrain the free disposal of those assets, whether movable or immovable, that form part of the assets of authorized assurance undertakings.

3. Paragraphs 1 and 2 shall not preclude any measures which Member States, while safeguarding the interests of the lives assured, are entitled to take as owners or members of or partners in the undertakings in question.'

Chapter 3

Article 28

The Member State of the commitment shall not prevent a policy-holder from concluding a contract with an assurance undertaking authorized under the conditions of Article 6 of Directive 79/267/EEC, as long as that does not conflict with legal provisions protecting the general good in the Member State of the commitment.

Article 29

Member States shall not adopt provisions requiring the prior approval or systematic notification of general and special policy conditions, scales of premiums, technical bases used in particular for calculating scales of premiums and technical provisions or forms and other printed documents which an assurance undertaking intends to use in its dealings with policy-holders.

Notwithstanding the first subparagraph, for the sole purpose of verifying compliance with national provisions concerning actuarial principles, the Member State of origin may require systematic communication of the technical Bases used in particular for calculating scales of premiums and technical provisions, without that requirement constituting a prior condition for an undertaking to carry on its business.

Not later than five years after the date of application of this Directive, the Commission shall submit a report to the Council on the implementation of those provisions.

Article 30

1. In the first subparagraph of Article 15 (1) of Directive 90/619/EEC the words 'in one of the cases referred to in Title III' shall be deleted.

2. Article 15 (2) of Directive 90/619/EEC shall be replaced by the following:

'2. The Member States need not apply paragraph 1 to contracts of six months' duration or less, nor where, because of the status of the policy-holder or the circumstances in which the contract is concluded, the policy-holder does not need this special protection. Member States shall specify in their rules where paragraph 1 is not applied.'

Article 31

1. Before the assurance contract is concluded, at least the information listed in point A of Annex II shall be communicated to the policy-holder.

2. The policy-holder shall be kept informed throughout the term of the contract of any change concerning the information listed in point B of Annex II.

3. The Member State of the commitment may require assurance undertakings to furnish information in addition to that listed in Annex II only if it is necessary for a proper understanding by the policy-holder of the essential elements of the commitment.

4. The detailed rules for implementing this Article and Annex II shall be laid down by the Member State of the commitment.

TITLE IV

PROVISIONS RELATING TO RIGHT OF ESTABLISHMENT AND FREEDOM TO PROVIDE SERVICES

Article 32

Article 10 of Directive 79/267/EEC shall be replaced by the following:

'*Article 10*

1. An assurance undertaking that proposes to establish a branch within the territory of another Member State shall notify the competent authorities of its home Member State.

2. The Member States shall require every assurance undertaking that proposes to establish a branch within the territory of another Member State to provide the following information when effecting the notification provided for in paragraph 1:

(a) the Member State within the territory of which it proposes to establish a branch;

(b) a scheme of operations setting out *inter alia* the types of business envisaged and the structural organization of the branch;

(c) the address in the Member State of the branch from which documents may be obtained and to which they may be delivered, it being understood that that address shall be the one to which all communications to the authorized agent are sent;

(d) the name of the branch's authorized agent, who must possess sufficient powers to bind the undertaking in relation to third parties and to represent it in relations with the authorities and courts of the Member State of the branch. With regard to Lloyd's, in the event of any litigation in the Member State of the branch arising out of underwritten commitments, the assured persons must not be treated less favourably than if the litigation had been brought against businesses of a conventional type. The authorized agent must, therefore, possess sufficient powers for proceedings to be taken against him and must in that capacity be able to bind the Lloyd's underwriters concerned.

3. Unless the competent authorities of the home Member State have reason to doubt the adequacy of the administrative structure or the financial situation of the assurance undertaking or the good repute and professional qualification or experience of the directors or managers or the authorized agent, taking into account the business planned, they shall within three months of receiving all the information referred to in paragraph 2 communicate that information to the competent authorities of the Member State of the branch and shall inform the undertaking concerned accordingly.

The competent authorities of the home Member State shall also attest that the assurance undertaking has the minimum solvency margin calculated in accordance with Articles 19 and 20.

Where the competent authorities of the home Member State refuse to communicate the information referred to in paragraph 2 to the competent authorities of the Member State of the branch they shall give the reasons for their refusal to the undertaking concerned within three months of receiving all the information in question. That refusal or failure to act shall be subject to a right to apply to the courts in the home Member State.

4. Before the branch of an assurance undertaking starts business, the competent authorities of the Member State of the branch shall, within two months of receiving the information referred to in paragraph 3, inform the competent authority of the home Member State, if appropriate, of the conditions under which, in the interest of the general good, that business must be carried on in the Member State of the branch.

5. On receiving a communication from the competent authorities of the Member State of the branch or, if no communication is received from them, on expiry of the period provided for in paragraph 4, the branch may be established and start business.

6. In the event of a change in any of the particulars communicated under paragraph 2 (b), (c) or (d), an assurance undertaking shall give written notice of the change to the competent authorities of the home Member State and of the Member State of the branch at least one month before making the change so that the competent authorities of the home Member State and the competent authorities of the Member State of the branch may fulfil their respective roles under paragraphs 3 and 4.'

Article 33

Article 11 of Directive 79/267/EEC shall be deleted.

Article 34

Article 11 of Directive 90/619/EEC shall be replaced by the following:

'Article 11

Any undertaking that intends to carry on business for the first time in one or more Member States under the freedom to provide services shall first inform the competent authorities of the home Member State, indicating the nature of the commitments it proposes to cover.'

Article 35

Article 14 of Directive 90/619/EEC shall be replaced by the following:

'Article 14

1. Within one month of the notification provided for in Article 11, the competent authorities of the home Member State shall communicate to the Member State or Member States within the territory of which the undertaking intends to carry on business by way of the freedom to provide services:

(a) a certificate attesting that the undertaking has the minimum solvency margin calculated in accordance with Articles 19 and 20 of Directive 79/267/EEC;

(b) the classes which the undertaking has been authorized to offer;

(c) the nature of the commitments which the undertaking proposes to cover in the Member State of the provision of services.

At the same time, they shall inform the undertaking concerned accordingly.

2. Where the competent authorities of the home Member State do not communicate the information referred to in paragraph 1 within the period laid down, they shall give the reasons for their refusal to the undertaking within that same period. The refusal shall be subject to a right to apply to the courts in the home Member State.

3. The undertaking may start business on the certified date on which it is informed of the communication provided for in the first subparagraph of paragraph 1.'

Article 36

Article 17 of Directive 90/619/EEC shall be replaced by the following:

'Article 17

Any change which an undertaking intends to make to the information referred to in Article 11 shall be subject to the procedure provided for in Articles 11 and 14.'

Article 37

Articles 10, 12, 13, 16, 22 and 24 of Directive 90/619/EEC shall be deleted.

Article 38

The competent authorities of the Member State of the branch or the Member State of the provision of services may require that the information which they are authorized under this Directive to request with regard to the business of assurance undertakings operating in the territory of that State shall be supplied to them in the official language or languages of that State.

Article 39

1. Article 19 of Directive 90/619/EEC shall be deleted.

2. The Member State of the branch or of provision of services shall not lay down provisions requiring the prior approval or systematic notification of general and special policy conditions, scales of premiums, technical bases used in particular for calculating scales of premiums and technical provisions, forms and other printed documents which an undertaking intends to use in its dealings with policy-holders. For the purpose of verifying compliance with national provisions concerning assurance contracts, it may require an undertaking that proposes to carry on assurance business within its territory, under the right of establishment or the freedom to provide services, to effect only non-systematic notification of those policy conditions

and other printed documents without that requirement constituting a prior condition for an undertaking to carry on its business.

Article 40

1. Article 20 of Directive 90/619/EEC shall be deleted.

2. Any undertaking carrying on business under the right of establishment or the freedom to provide services shall submit to the competent authorities of the Member State of the branch and/or of the Member State of the provision of services all documents requested of it for the purposes of this Article in so far as undertakings the head office of which is in those Member States are also obliged to do so.

3. If the competent authorities of a Member State establish that an undertaking with a branch or carrying on business under the freedom to provide services in its territory is not complying with the legal provisions applicable to it in that State, they shall require the undertaking concerned to remedy that irregular situation.

4. If the undertaking in question fails to take the necessary action, the competent authorities of the Member State concerned shall inform the competent authorities of the home Member State accordingly. The latter authorities shall, at the earliest opportunity, take all appropriate measures to ensure that the undertaking concerned remedies that irregular situation. The nature of those measures shall be communicated to the competent authorities of the Member State concerned.

5. If, despite the measures taken by the home Member State or because those measures prove inadequate or are lacking in that State, the undertaking persists in violating the legal provisions in force in the Member State concerned, the latter may, after informing the competent authorities of the home Member State, take appropriate measures to prevent or penalize further irregularities, including, in so far as is strictly necessary, preventing that undertaking from continuing to conclude new assurance contracts within its territory. Member States shall ensure that in their territories it is possible to serve the legal documents necessary for such measures on assurance undertakings.

6. Paragraphs 3, 4 and 5 shall not affect the emergency power of the Member States concerned to take appropriate measures to prevent or penalize irregularities committed within their territories. This shall include the possibility of preventing assurance undertakings from continuing to conclude new assurance contracts within their territories.

7. Paragraph 3, 4 and 5 shall not affect the power of the Member States to penalize infringements within their territories.

8. If an undertaking which has committed an infringement has an establishment or possesses property in the Member State concerned, the competent authorities of the latter may, in accordance with national law, apply the administrative penalties prescribed for that infringement by way of enforcement against that establishment or property.

9. Any measure adopted under paragraphs 4 to 8 involving penalties or restrictions on the conduct of assurance business must be properly reasoned and communicated to the undertaking concerned.

10. Every two years, the Commission shall submit to the Insurance Committee a report summarizing the number and type of cases in which, in each Member State, authorization has been refused pursuant to Article 10 of Directive 79/267/EEC or Article 14 of Directive 90/619/EEC as amended by this Directive or measures have been taken under paragraph 5. Member States shall cooperate with the Commission by providing it with the information required for that report.

Article 41

Nothing in this Directive shall prevent assurance undertakings with head offices in other Member States from advertising their services through all available means of communication in the Member State of the branch or Member State of the provision of services, subject to any rules governing the form and content of such advertising adopted in the interest of the general good.

Article 42

1. Article 21 of Directive 90/619/EEC shall be deleted.

2. Should an assurance undertaking be wound up, commitments arising out of contracts underwritten through a branch or under the freedom to provide services shall be met in the same way as those arising out of that undertaking's other assurance contracts, without distinction as to nationality as far as the lives assured and the beneficiaries are concerned.

Article 43

1. Article 23 of Directive 90/619/EEC shall be deleted.

2. Every assurance undertaking shall inform the competent authority of its home Member State, separately in respect of transactions carried out under the right of establishment and those carried out under the freedom to

provide services, of the amount of the premiums, without deduction of reassurance, by Member State and by each of classes I to IX, as defined in the Annex to Directive 79/267/EEC.

The competent authority of the home Member State shall, within a reasonable time and on an aggregate basis forward this information to the competent authorities of each of the Member States concerned which so request.

Article 44

1. Article 25 of Directive 90/619/EEC shall be deleted.

2. Without prejudice to any subsequent harmonization, every assurance contract shall be subject exclusively to the indirect taxes and parafiscal charges on assurance premiums in the Member State of the commitment within the meaning of Article 2 (e) of Directive 90/619/EEC and also, with regard to Spain, to the surcharges legally established in favour of the Spanish 'Consorcio de compensación de seguros' for the performance of its functions relating to the compensation of losses arising from extraordinary events occurring in that Member State.

The law applicable to the contract pursuant to Article 4 of Directive 90/619/EEC shall not affect the fiscal arrangements applicable.

Pending future harmonization, each Member State shall apply to those undertakings which cover commitments situated within its territory its own national provisions for measures to ensure the collection of indirect taxes and parafiscal charges due under the first subparagraph.

TITLE V

TRANSITIONAL PROVISIONS

Article 45

Member States may allow assurance undertakings with head offices in their territories, and whose buildings and land covering their technical provisions exceed, at the time of the notification of this Directive, the percentage laid down in Article 22 (1) (a) a period expiring no later than 31 December 1998 within which to comply with that provision.

Article 46

1. Article 26 of Directive 90/619/EEC shall be deleted.

2. Spain and Portugal, until 31 December 1995, and Greece, until 31 December 1998, may operate the following transitional arrangements for contracts in respect of which one of those Member States is the Member State of the commitment:

(a) by way of derogation from Article 8 (3) of Directive 79/267/EEC and from Articles 29 and 39 of this Directive, the competent authorities of the Member States in question may require the communication, before use, of general and special insurance policy conditions;

(b) the amount of the technical provisions relating to such contracts shall be determined under the supervision of the Member State concerned in accordance with its own rules or, failing that, in accordance with the procedures established in that State in accordance with this Directive. Cover of those technical provisions by equivalent and matching assets and the localization of those assets shall be effected under the supervision of that Member State in accordance with its rules and practices adopted in accordance with this Directive.

TITLE VI

FINAL PROVISIONS

Article 47

The following technical adjustments to be made to Directives 79/267/EEC and 90/619/EEC and to this Directive shall be adopted in accordance with the procedure laid down in Directive 91/675/EEC:

— extension of the legal forms provided for in Article 8 (1) (a) of Directive 79/267/EEC,

— amendments to the list set out in the Annex to Directive 79/267/EEC, or adaptation of the terminology used in that list to take account of the development of assurance markets,

— clarification of the items constituting the solvency margin listed in Article 18 of Directive 79/267/EEC to take account of the creation of new financial instruments,

— alteration of the minimum guarantee fund provided for in Article 20 (2) of Directive 79/267/EEC to take account of economic and financial developments,

— amendments, to take account of the creation of new financial instruments, to the list of assets acceptable as cover for technical provisions set out in Article 21 of this Directive and to the rules on the spreading of investments laid down in Article 22 of this Directive,

— changes in the relaxations in the matching rules laid down in Annex I to this Directive, to take account of the development of new currency-hedging instruments or progress made in economic and monetary union,

— clarification of the definitions in order to ensure uniform application of Directives 79/267/EEC and 90/619/EEC and of this Directive throughout the Community,

— the technical adjustments necessary to the rules for setting the maxima applicable to interest rates, pursuant to Article 17 of Directive 79/267/EEC, as amended by this Directive, in particular to take account of progress made in economic and monetary union.

Article 48

1. Branches which have started business, in accordance with the provisions in force in their Member State of establishment, before the entry into force of the provisions adopted in implementation of this Directive shall be presumed to have been subject to the procedure laid down in Article 10 (1) to (5) of Directive 79/267/EEC. They shall be governed, from the date of that entry into force, by Articles 17, 23, 24 and 26 of Directive 79/267/EEC and by Article 40 of this Directive.

2. Articles 11 and 14 of Directive 90/619/EEC, as amended by this Directive, shall not affect rights acquired by assurance undertakings carrying on business under the freedom to provide services before the entry into force of the provisions adopted in implementation of this Directive.

Article 49

The following Article 31a shall be inserted in Directive 79/267/EEC:

'Article 31a

1. Under the conditions laid down by national law, each Member State shall authorize agencies and branches set up within its territory and covered by this Title to transfer all or part of their portfolios of contracts to an accepting office established in the same Member State if the competent authorities of that Member State or, if appropriate, those of the Member State referred to in Article 30 certify that after taking the transfer into account the accepting office possesses the necessary solvency margin.

2. Under the conditions laid down by national law, each Member State shall authorize agencies and branches set up within its territory and covered by this Title to transfer all or part of their portfolios of contracts to an assurance undertaking with a head office in another Member State if the competent authorities of that Member State certify that after taking the transfer into account the accepting office possesses the necessary solvency margin.

3. If under the conditions laid down by national law a Member State authorizes agencies and branches set up within its territory and covered by this Title to transfer all or part of their portfolios of contracts to an agency or branch covered by this Title and set up within the territory of another Member State it shall ensure that the competent authorities of the Member State of the accepting office or, if appropriate, of the Member State referred to in Article 30 certify that after taking the transfer into account the accepting office possesses the necessary solvency margin, that the law of the Member State of the accepting office permits such a transfer and that the State has agreed to the transfer.

4. In the circumstances referred to in paragraphs 1, 2 and 3 the Member State in which the transferring agency or branch is situated shall authorize the transfer after obtaining the agreement of the competent authorities of the Member State of the commitment, where different from the Member State in which the transferring agency or branch is situated.

5. The competent authorities of the Member States consulted shall give their opinion or consent to the competent authorities of the home Member State of the transferring assurance undertaking within three months of receiving a request; the absence of any response from the authorities consulted within that period shall be considered equivalent to a favourable opinion or tacit consent.

6. A transfer authorized in accordance with this Article shall be published as laid down by national law in the Member State of the commitment. Such transfers shall automatically be valid against policy-holders, assured persons and any other persons having rights or obligations arising out of the contracts transferred.

This provision shall not affect the Member States' right to give policy-holders the opinion of cancelling contracts within a fixed period after a transfer.'

Article 50

Member States shall ensure that decisions taken in respect of an assurance undertaking under laws, regulations and administrative provisions adopted in accordance with this Directive may be subject to the right to apply to the courts.

Article 51

1. Member States shall adopt the laws, regulations and administrative provisions necessary for their compliance with this Directive no later than 31 December 1993 and

bring them into force no later than 1 July 1994. They shall forthwith inform the Commission thereof.

When they adopt such measures, the Member States shall include references to this Directive or shall make such references when they effect official publication. The manner in which such references are to be made shall be laid down by the Member States.

2. The Member States shall communicate to the Commission the texts of the main provisions of national law which they adopt in the field covered by this Directive.

Article 52

This Directive is addressed to the Member States.

Done at Brussels, 10 November 1992.

For the Council

The President

R. NEEDHAM

ANNEX I

MATCHING RULES

The currency in which the assurer's commitments are payable shall be determined in accordance with the following rules:

1. Where the cover provided by a contract is expressed in terms of a particular currency, the assurer's commitments are considered to be payable in that currency.

2. Member States may authorize undertakings not to cover their technical provisions, including their mathematical provisions, by matching assets if application of the above procedures would result in the undertaking being obliged, in order to comply with the matching principle, to hold assets in a currency amounting to not more than 7% of the assets existing in other currencies.

3. Member States may choose not to require undertakings to apply the matching principle where commitments are payable in a currency other than the currency of one of the Community Member States, if investments in that currency are regulated, if the currency is subject to transfer restrictions or if, for similar reasons, it is not suitable for covering technical provisions.

4. Undertakings are authorized not to hold matching assets to cover an amount not exceeding 20% of their commitments in a particular currency.

   However, total assets in all currencies combined must be at least equal to total commitments in all currencies combined.

5. Each Member State may provide that, whenever under the preceding procedures a commitment has to be covered by assets expressed in the currency of a Member State, this requirement shall also be considered to be satisfied when the assets are expressed in ecus.

ANNEX II

INFORMATION FOR POLICY-HOLDERS

The following information, which is to be communicated to the policy-holder before the contract is concluded (A) or during the term of the contract (B), must be provided in a clear and accurate manner, in writing, in an official language of the Member State of the commitment.

However, such information may be in another language if the policy-holder so requests and the law of the Member State so permits or the policy-holder is free to choose the law applicable.

A. Before concluding the contract

Information about the assurance undertaking	Information about the commitment
(a) 1. The name of the undertaking and its legal form	(a) 4. Definition of each benefit and each option
(a) 2. The name of the Member State in which the head office and, where appropriate, the agency or branch concluding the contract is situated	(a) 5. Term of the contract
(a) 3. The address of the head office and, where appropriate, of the agency or branch concluding the contract	(a) 6. Means of terminating the contract
	(a) 7. Means of payment of premiums and duration of payments
	(a) 8. Means of calculation and distribution of bonuses
	(a) 9. Indication of surrender and paid-up values and the extent to which they are guaranteed
	(a) 10. Information on the premiums for each benefit, both main benefits and supplementary benefits, where appropriate
	(a) 11. For unit-linked policies, definition of the units to which the benefits are linked
	(a) 12. Indication of the nature of the underlying assets for unit-linked policies
	(a) 13. Arrangements for application of the cooling-off period
	(a) 14. General information on the tax arrangements applicable to the type of policy
	(a) 15. The arrangements for handling complaints concerning contracts by policy-holders, lives assured or beneficiaries under contracts including, where appropriate, the existence of a complaints body, without prejudice to the right to take legal proceedings
	(a) 16. Law applicable to the contract where the parties do not have a free choice or, where the parties are free to choose the law applicable, the law the assurer proposes to choose

B. During the term of the contract

In addition to the policy conditions, both general and special, the policy-holder must receive the following information throughout the term of the contract.

Information about the assurance undertaking	Information about the commitment
(b) 1. Any change in the name of the undertaking, its legal form or the address of its head office and, where appropriate, of the agency or branch which concluded the contract	(b) 2. All the information listed in points (a) (4) to (a) (12) of A in the event of a change in the policy conditions or amendment of the law applicable to the contract. (b) 3. Every year, information on the state of bonuses