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TOWARD A COMMON MARKET IN LIFE INSURANCE

A common market for life insurance is now being developed in the nine-nation European Community. The foreign ministers of Belgium, Britain, Denmark, France, Germany, Ireland, Italy, Luxembourg and the Netherlands took an important step toward this goal last month by issuing a directive ordering the EC nations to align their national laws, regulations and administrative procedures with uniform Community rules for setting up and conducting the life insurance business.

$22.4 BILLION BUSINESS

This directive calls for identical conditions for establishment in all member states -- whether head office, agency or branch -- and identical conditions for carrying out business. Its aim is to protect the insured and to create a favorable climate for competition by getting rid of diverse supervisory rules and requirements. The importance of the life insurance business can be seen from the fact that in 1976 the industry was responsible for about $22.4 billion in business turnover in the nine EC nations.

The new directive gives any life insurance company with a head office in a Community country the right to establish an agency or branch in any other EC nation. It is similar to a directive adopted by the Council in July 1973 that coordinated the activities of non-life insurance companies. This life insurance directive was, in

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fact, proposed shortly after common rules for risk insurance were accepted. Delay was occasioned by lack of agreement on how companies should be structured and how guarantees of financial viability should be figured.

COMPANIES MUST SPECIALIZE

In four EC countries -- France, Germany, Ireland and the Netherlands -- companies specialize in one category of insurance only. They may not deal in both life and indemnity coverage. The laws of two member states -- Denmark and Italy -- encourage specialization but do not require it for pre-existing composite companies. In three others -- Britain, Belgium and Luxembourg -- companies can offer a variety of services.

The question of which structure to adopt for the Community was resolved by allowing composite companies to continue to write both life and indemnity policies indefinitely, with the provision that they adopt strict rules on separate management of the two. A composite company will have to set up a separate subsidiary for life insurance to operate in another member country. Any undertaking set up after the entry into force of the directive must specialize; no new companies will be allowed to deal in both life and risk insurance.

SUPPLEMENTARY RESERVE

The problem of financial guarantees resulted from national differences in handling assets and in calculating reserves. For one thing, composite companies can easily switch their assets from one category of insurance to another. With specialized companies, risks are not so widely spread. To make sure the consumer will be protected by both types of undertakings, the Community directive requires not only guarantees of proof of technical reserves but an additional financial reserve asset called a solvency margin. This supplementary reserve in prescribed amounts is to be calculated on the amount of paid-up share capital included in the company's balance sheet and on future profits, predicted on the basis of the company's profits over the previous five years.

Financial supervision for the entire activity of an undertaking is provided in the same way as in the earlier directive on risk insurance. Authorities of the member countries in which the head office is located, with assistance from authorities in other countries where agencies or branches are set up, will be responsible for supervising a company's finances.

The directive on life insurance also takes into account agreements with countries outside the Community. In order to ensure, on a reciprocal basis, that policyholders are adequately protected, provisions may differ from those laid down for the member countries.

Formal adoption of the directive is expected shortly. It will then be published in the six languages of the Community. Member states will then have a specific time to modify their national provisions and apply Community provisions.

OTHER DIRECTIVES ON INSURANCE

This is the latest in a number of steps that have been taken toward a common market in insurance. In addition to the 1973 directive on risk insurance, they include others concerning:

- 1964 - Reinsurance -- removing from national legislation provisions obstructing business in reinsurance;
- 1972 - Third party insurance for motor vehicles -- eliminating the need for showing a "green card" when crossing borders;
- 1972 - Activities of insurance brokers and agents;
- 1978 - Intra-Community co-insurance transactions -- coordinating laws, rules and administrative provisions.

The most important step, however, still remains to be taken. Officials will be working next on a directive to make it possible for indemnity insurers in member countries to sell their services freely across frontiers, regardless of in which EC country they are established. A directive on cross-frontier freedom for life insurance sales, expected to follow, would then mark the establishment of a complete common market in the insurance industry.