

COMMISSION OF THE EUROPEAN COMMUNITIES

COM(91) 55 final

Brussels, 22 February 1991

REPORT OF THE COMMISSION TO THE COUNCIL CONCERNING
THE OPERATIONS REFERRED TO IN DIRECTIVE 79/267/EEC OF THE
5TH MARCH 1979 AND UNDERTAKEN BY COMPOSITE AND SPECIALISED COMPANIES

**REPORT OF THE COMMISSION TO THE COUNCIL CONCERNING
THE OPERATIONS REFERRED TO IN DIRECTIVE 79/267/EEC OF THE
5TH MARCH 1979 AND UNDERTAKEN BY COMPOSITE AND SPECIALISED COMPANIES**

Introduction

The report

Article 39 paragraph 2 of directive 79/267/EEC of 5th March 1979 (subsequently referred to as the first life directive) says :

"Following a period of 10 years from the ratification of this directive, the Commission shall submit to the Council a report dealing with the operations of the two types of undertakings covered by this directive : that is to say, those undertakings which carry on simultaneously the activity covered by the first coordination directive (non-life insurance) in addition to the activity covered by this directive and those undertakings which carry on only the activity covered by this directive."

In addition, Article 18 of directive 90/619/EEC of 8th November 1990 (the second life directive) specifies the regime for free provision of services in life assurance which is to apply to composite companies. Paragraph 2 of this article reads as follows :

"This article will be reviewed in the light of the report to be prepared by the Commission in accordance with Article 39(2) of the first directive."

In accordance with these provisions, this report reviews :

- the operation of specialised companies in the Community since 1979 ;

- the application by Member States of the arrangements required for composite companies ;
- whether the restrictions of directive 79/267/EEC can still be justified.

The initial legal regime

The first life directive established a legal regime which at the time was intended to protect the interests not only of life assurance policyholders, but also of non-life policyholders. It was also intended to be a significant step forward in coordinating the requirements for authorisation and conduct of business in life assurance and in the creation of agencies and branches in other Community countries in a coordinated manner.

This directive established the principle of specialisation, that an insurance company can only carry out one of the two types of business, either life, or non-life business.

However, it restricted the application of this principle to new companies, by forbidding the creation of new composite companies. It allowed Member States either to permit existing composites to continue, or to require that they convert to specialised companies.

Some Member States, such as Germany, Greece and Denmark, have chosen to impose specialisation, but it is worth noting that they were not obliged to do so.

Some requirements were also laid down concerning the relationship between the life and non-life activities within a composite company or between separate but related life and non life companies. For the former, separate management and accounting were required, and for the latter the supervisory authorities were to ensure that the accounts of the companies concerned were not distorted by agreements between the companies or by any arrangement which could affect the apportionment of expenses and income.

The legal and economic environment

Any report which aims to review the management of composite and specialised companies in those activities covered by the first life directive, cannot be prepared 'in abstracto', but must take into account the changes since 1979 in the legal and economic environment for life assurance in the community.

- a) The overall programme for the completion of the single market by 31.12.1992, described and outlined in the 1985 White Paper, was approved by the Member States and incorporated into the Single European Act in 1986. This eased the adoption of the necessary texts in particular by extending the use of qualified majority voting. The emphasis is now on mutual recognition of the systems in different Member States and on the freedom of consumers to choose between products and companies throughout the Community.

In this perspective, the second life directive laid down the means for the introduction of free provision of services and the proposal for a third life assurance directive extends this freedom and creates the single licence system.

These important changes to the texts mean that it is necessary to examine closely whether the restrictions on composite companies are still justified.

- b) In the wider area of financial services, the last ten years have seen major developments in the direction of despecialisation, and the creation of large financial groups, often with very complex structures. This is certainly the case in the investment services sector, but also in the banking sector, where despecialisation has already been accepted in the 2nd banking coordination directive, which requires all Member States to allow access to their market for 'universal banks' approved in another Member State. The insurance sector has also been affected by similar developments. All sorts of different financial services may now be offered by different specialised companies within a group, or in some cases by a single company with separate managements or 'Chinese walls'.

In several countries, insurance companies that are subsidiaries of banks are taking an increasing market share in life assurance and financial groups are thus being formed covering several areas of financial services. Within a single group it is now possible to find companies offering life assurance, non-life assurance, banking services and stockbroking. The insurance products may actually be sold by a bank within the same group. The staff may be shared between the different companies, sometimes even employed by a separate company whose only activity is to provide services to the other group companies. The assets of the group companies may all be managed by a single company.

In parallel with these developments, technological progress in the last decade has made it much easier to operate systems of separate management and accounting for composite companies.

This kind of economic and technological development must be taken into account in reviewing the position of composite companies. It would not be appropriate for legislation to hinder a natural development of the market, if this is not necessary for prudential or consumer protection reasons.

The Second Life Directive of 8.11.1990

This directive gave full freedom for the provision of services in life assurance to existing composite companies until 31st December 1995. From this date, in the absence of any further legislation stemming from the report requested in the first Directive, composite companies would no longer be able to operate by free provision of services in those countries which are 'specialised'.

Preparation of the report

In order to prepare the required report, Directorate General XV sent out a questionnaire to the Member States in February and March 1990. Although satisfactory replies were received, they showed that the subject deserved a more thorough investigation. As a result, it was decided that a more detailed survey should be carried out by an independent body. The Commission Consultative des achats et marchés (C.C.A.M.) of the Commission chose Price Waterhouse from amongst the many bodies who indicated their availability for this type of survey.

This company carried out a large number of interviews with supervisory authorities and with the insurance industry representative bodies in all Member States in addition to submitting written questions.

The Commission would like to thank the many people in supervisory authorities and in professional associations who replied in person or in writing to the questions put by the consultants and who organised meetings with them.

The results of the survey

The consultants were particularly asked to look at the following questions :

- Are the current regulations sufficient for the control of composite companies ?
- Should they be either reinforced or relaxed ?
- Can the current restrictions on composite companies still be justified ?

A large amount of work was done by means of interviews, research and analysis, and this led to consideration of three major areas. These are the financial position of companies, the practical problems of allocating income and expenses in composite companies, and the problems of winding-up.

1. The financial position of life assurance companies

The first important observation is the very high level of financial security offered by companies offering life assurance products in the Community. Over a ten year period, out of the more than 4000 companies authorised within the Community, there have only been 4 cases of winding-up. All of these were specialised companies. There have been therefore no cases of winding-up of a composite company, although over the same period there have been several failures of specialised non-life companies. Overall it must be said that there are very few instances of failure.

There is then the more general question of whether composite or specialised life assurance companies have experienced financial difficulties. The replies of Member States show that in several cases, supervisory authorities have felt it necessary to intervene to ask for additional information or to take appropriate measures to deal with financial difficulties. However, these cases have been resolved efficiently without needing to invoke the procedures for withdrawing authorisation.

These observations, which are covered in more detail in the consultants' report, show that :

- the control systems in life assurance, based on the system of prevention and resolution of problems, set out in the first directive, but organised in different ways in different Member States, have proved their effectiveness over the last ten years.

- life assurance policyholders with a composite company, together with lives assured and beneficiaries, are no less well protected than with a specialised company.

2. The practical working of the arrangements for composite companies imposed by the first directive

In order to protect the interests of life policyholders within a composite company, the first life directive required such companies to adopt separate management and accounting and in particular to separate all income and expenses as appropriate between the life and non-life branches. It also laid down strict rules regarding the transfer of solvency margins between the life and non-life sectors of a composite company.

In general the regime laid down for composite companies by the first life directive appears to have worked well. All the Member States have correctly implemented the requirements in their legislation and there have been no major difficulties in installing separate management and accounting systems in composite companies. The possibility of transferring the solvency margin between the life and non-life sectors has been used rarely; where it has been used, no difficulties have occurred.

However, several Member States did indicate some difficulty in the allocation of items to one sector or the other, not as a result of the European regulations, which seem to be sufficiently precise, but simply on a practical level.

The split of items between the two sectors and the control of this allocation can indeed be very complex, because distribution channels, computer installations, investment departments and even the administrative staff are often shared between the two sectors.

However, this problem is not peculiar to composite companies and occurs in just the same way where two specialised companies, one in life, the other in non-life, belong to the same group. In this case there is also the risk that the accounts of the companies could be distorted by agreements between them or by any arrangement which could influence the allocation of income and expenses. This possibility is foreseen explicitly by Article 13, paragraph 2 of the first life directive.

The requirements for separate management have also led to cooperation between supervisory authorities in the Community. This has taken the form of exchanges of view and communication of the national texts applying, within the framework of the Conference of Insurance Supervisory Authorities of the EEC countries.

This Conference does indeed seem to be the appropriate body to tackle these practical problems.

3. The problems of winding-up of life assurance companies

Although the statistics show that the risk of winding-up of either a composite company or a specialist life assurance company is very small, as a result of the general economic environment and the existence of a well-organised supervisory system, amongst other factors, it is nevertheless important to consider the position of life policyholders in the event of a winding-up.

In the event of a winding-up of a composite company, full separation of assets and proper allocation of income and expenditure would be of great importance to ensure the contractual rights of policyholders. However, as the report shows, these practical questions are not confined to composite companies but also concern specialised companies, in particular when they form part of a group. It is also necessary to ensure that the assets covering life policyholders' liabilities are allocated to life policyholders, and that they have as high a ranking as possible in their claim on other assets, and in particular rank above the unsecured creditors of the insurance company.

All of these questions are part of a wider problem, that is whether policyholders are sufficiently protected in the event of the winding-up of an insurance company. These issues should therefore be examined in the context of the proposal for a directive concerning the winding-up of insurance companies (Amended Commission proposal of 18th September 1989 - O.J. N° C 253 of 6th October 1989). Taking into account the very limited number of cases of winding-up during the period considered in the report, this should however not be regarded as a prior condition for reviewing the current position of composite companies.

Conclusions

These observations and analyses lead to the following conclusions :

1. The current rules on separate management and accounting are being correctly and seem to be sufficient. It does not seem necessary either to reinforce or to relax them.
2. There is no evidence that the system of specialisation may offer in practice greater protection to life policyholders than the composite system.

There is therefore no justification for maintaining the current restrictions on composite companies either in respect of the freedom of establishment or free provision of services.

- a) Composite companies should therefore be allowed to create composite branches and agencies throughout the Community.

- b) Similarly, they should be able to operate by free provision of services throughout the Community, even after 31st December 1995.

- c) For the same reasons, it also seems necessary to lift the current ban on the creation of new composite companies, or at least allow Member States to lift this restriction for companies created within their territory.

COM(91) 55 final

DOCUMENTS

EN

10 08

Catalogue number : CB-CO-91-070-EN-C
ISBN 92-77-69454-8

PRICE	1 - 30 pages: 3.50 ECU	per additional 10 pages: 1.25 ECU
-------	------------------------	-----------------------------------

Office for Official Publications of the European Communities
L-2985 Luxembourg