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**Commission inquiry into**
**the European business insurance sector**

Comments of Assuralia on the Interim Report

## Assuralia Profile

Founded in 1920, Assuralia is legally and widely recognised as the representative body for more than 90 mutual and joint-stock insurance companies in Belgium, covering about 95% of the Belgian market and 33.833 million euro gross premium income in 2005 (local business excluding FOS premium and RE premium income). Assuralia represents the interests of the insurers active on the Belgian market. It is a member of the Comité Européen des Assurances (CEA).

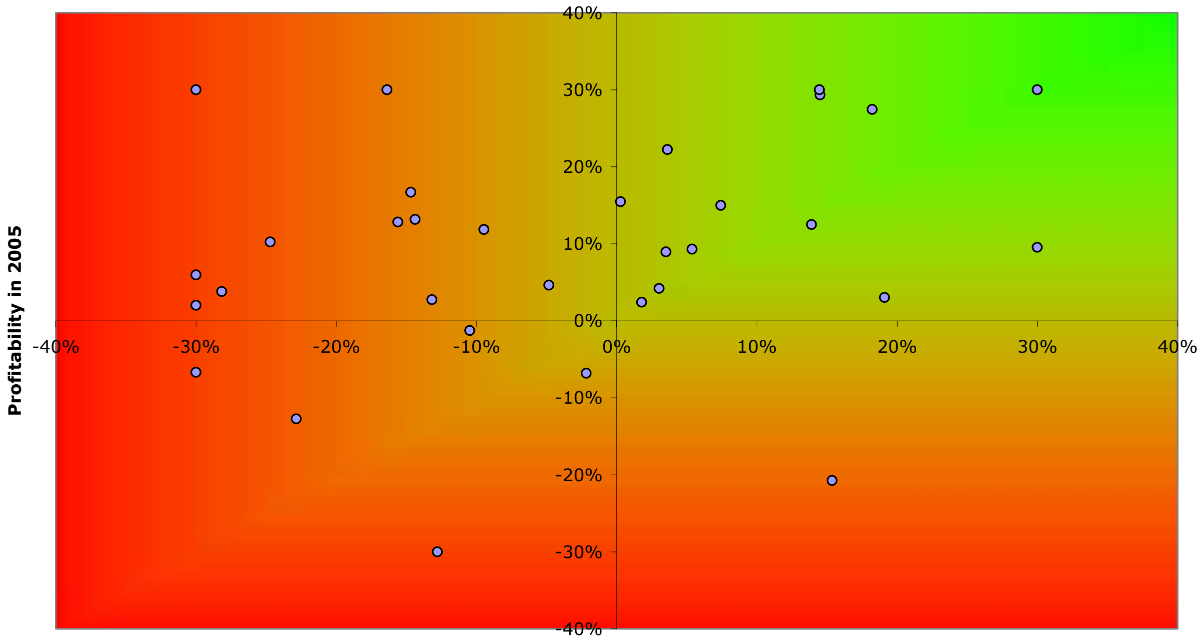
## I. General remark

Assuralia welcomes the opportunity to engage in a constructive dialogue on the preliminary findings of the Sector Inquiry presented by DG Competition in the Interim Report. In Assuralia's view, the report could be improved by better taking into account the dynamics of the Belgian insurance market, on the one hand, and, on the other hand, the advantages of horizontal cooperation between insurance companies as covered by the Block exemption Regulation (BER). This paper focuses on issues and questions with specific relevance for the Belgian market, referring to the response of CEA for other comments.

## II. Financial aspects

The Interim Report measures market profitability by means of combined ratios, loss ratios, expense ratios and net investment results. It flags three specific issues that may point to restrictive market conditions on the Belgian market. Assuralia believes that this does not entirely reflects reality. Graph n°1 illustrates how profitability in fire insurance for example varies strongly among insurance companies on the Belgian market.

**Graph 1. Profitability Fire Insurance**




**Profitability in 2002**

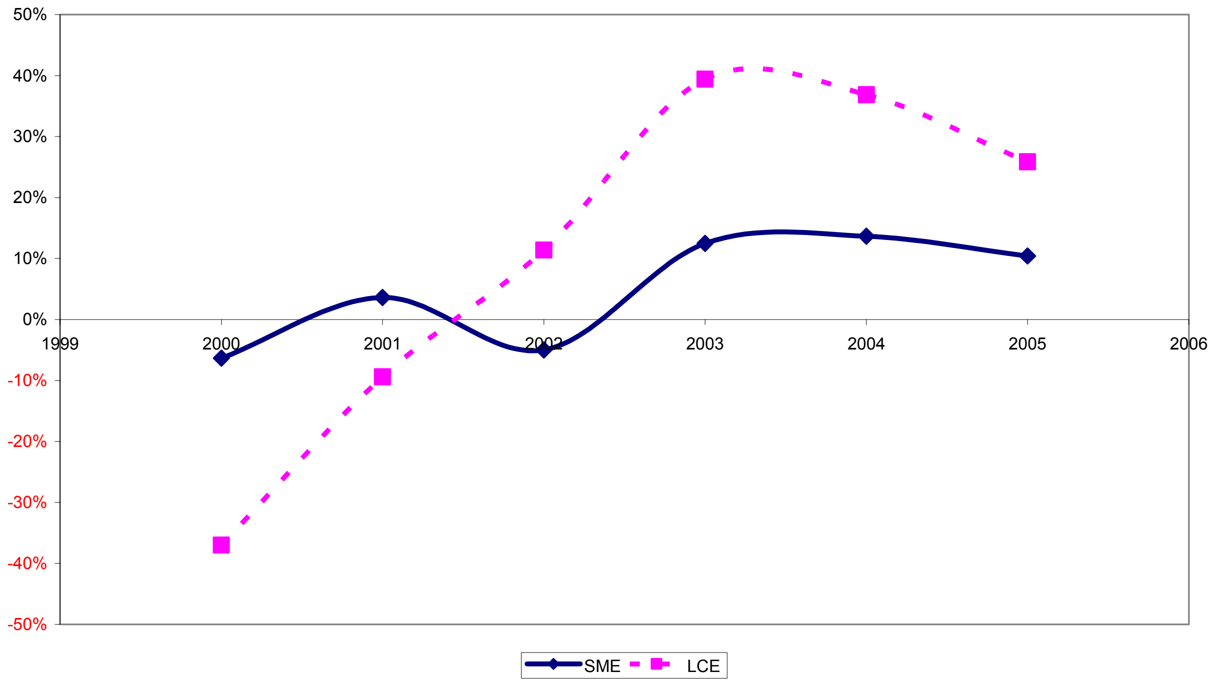
The Report states that a relatively high degree of sustained profitability in a mature market, measured by means of combined ratios, could be an indicator for market power abuse. We believe combined ratios must be examined over significant periods of time and in conjunction with investment profitability and reinsurance premiums paid. Good investment results allow insurance companies to accept underwriting losses to a certain extent, particularly in long-tail business. Important investment losses however push insurance companies to go back to more balanced technical results and to improve underwriting profitability in general. We believe the positive underwriting results of the last years must be seen in contrast with the financial crisis in the beginning of this decade.

The Interim Report suggests as well that different combined ratios between insurance lines indicate that profits in some lines are used to subsidise losses in other lines. This argument is waived by the prohibition of the Belgian insurance supervisory authority CBFA to cross-subsidize between insurance product lines. In contrast with the supervisory culture in a number of other member states, in Belgium each separate insurance product line must be structurally profitable to safeguard the companies' solvency in the long run.

Finally, the Interim Report shows that combined ratios for business insurance in Belgium have consistently been higher for small and medium sized companies than for large companies in the period 2000 to 2005. Profit margins in the Belgian business insurance market have thus not caused competitive advantages for LCCs to the detriment of SME's over the last years. Assuralia would like to suggest the Commission to take into account, first, the fact that insuring LCCs usually requires heavier reinsurance and capital requirements from the direct insurer. Secondly, the bargaining power of LCCs on the insurance market may have an important effect on the volatility of the combined ratios concerning LCC insurance as well. This is reflected for fire insurance[1] in Graph n° 2.

[1] Fire insurance is the only branch for which Assuralia can accurately distinguish statistics for LCCs and SMEs.

**Graph 2. Profitability Fire Insurance (in % of premiums)**




## III. The duration of insurance contracts

The Interim Report rightly states that the use of annual contracts is a general practice in many a member state, including Belgium. Such short duration is widely believed to foster competition between insurance companies. It is important to understand that while short term contracts may generate certain specific benefits, contracts of longer duration may generate others.

Contracts of longer duration do for example allow businesses and insurance companies to cooperate in the field of prevention and to create win-win situations. Prevention is beneficial to both insurance companies (reduction of claims) and enterprises (reduction of premiums). Enterprises engage more easily in investing in preventive measures if they are assured that their insurance premiums will be reduced over a longer period of time.

Insurance contracts, that match the duration of prevention cost recovery, facilitate beneficial collaboration. As a rare exception, recent Belgian legislation expressly allows enterprises to purchase three year policies for workmen's compensation insurance. These contracts are accompanied by prevention programmes, often supported by the prevention experts of the insurance company.

## IV. Insurance intermediaries

As a general remark, Assuralia would like to point out that there is a high degree of competition on the Belgian insurance market, both between various distribution channels and among insurance intermediaries. Market efficiency is well served by the diversity of the distribution channels presently available to customers and to insurance companies. The conclusions of the report should not lead to a reduction of this diversity or to excessive requirements.

The Insurance Mediation Directive (IMD) already defines transparency rules for insurance intermediaries.[2] It provides for a clear understanding of the status of the intermediary as meant by this directive as well as of the nature of the advice he offers. The directive deserves more time – certainly if the perception by the end-user is to be used as a reference - to prove its added value with regard to transparency and conflict of interest resolution. In line with the Better Regulation approach, the European Commission may want to appraise the practical results of the IMD over the next years, before engaging in new legislative reform.

Assuralia is not aware of existing agreements between insurers and independent intermediaries not to rebate commissions to insurance broking clients. It may be of interest to the Commission that Assuralia and the Belgian federations of insurance intermediaries have published codes of conduct in order to further, among other objectives, transparency of insurance intermediation, in the interest of the consumer (http://www.assuralia.be/nl/rules/index.asp).

## V. Differences between Member states regarding horizontal cooperation

In view of the expiration of the Block Exemption Regulation (BER) on 31st March 2010, the Commission is asking the insurance industry to bring forward the merits of the BER in today's insurance market. The Interim Report points out that the various forms of cooperation among insurers show substantial differences among Member States. These differences have raised doubts on the usefulness of the BER for today's insurance market and the insurance industry is invited to bring forward convincing explanations.

It goes without saying that the deadline for commenting on the Interim Report is too tight to set up a thorough analysis to explain the differences found among member states. Assuralia disagrees however, with the reasoning that one can reasonably deduct from the sole fact that differences exist between member states, that the BER is no longer useful. In Belgium, horizontal cooperation covered by the BER has proven beneficial to customers, insurers and society.

There are valid reasons to continue to use this option and to renew the existing BER beyond 2010. The BER avoids unnecessary legal compliance costs by offering a 'safe harbour' in well defined situations. It is an important and useful tool for the assessment of the activities of insurance companies, professional associations and governments and offers legal security.

The horizontal cooperation cleared by the BER actually fosters competition. Assuralia is sincerely concerned that, without such clarity, establishing positive business cooperation would become difficult or even abandoned. Business cooperation in the field of joint calculations and pools are excellent examples.

### *Joint calculations, tables and studies*

Any insurer seeks to reduce as much as possible divergence between, on the one hand, the unknown real value of a future claim for which the costumer will have to be compensated and, on the other hand, the premiums paid to get insurance cover. To this end, the insurer defines homogenous risk groups and calculates their average cost on the basis of statistics. The BER ensures that insurers are allowed to improve their statistical data by jointly undertaking studies.[3] High quality statistics allow for precise calculations and low security

[2] Directive 2002/92/EC of the European Parliament and of the Council of 9 December 2002 on insurance mediation, OJ L 009 , 15th January 2003.
[3] COM (1999), 192, p. 3.

margins for risks, especially the most volatile ones. Without such cooperation, premiums would increase to the detriment of consumers.

Assuralia emphasises that new entrants, big players and smaller players on the Belgian insurance market benefit from the risk data shared by the Belgian insurance industry. These data are accessible to all companies, including insurance provided in FOS, at conditions that are not discriminatory. Without access to these aggregated data, the costs of entering the Belgian market would be significantly higher, because of the need to take into account higher security margins when calculating premiums.

Differences between national markets in this field may originate from differences in the field of legislation or differences regarding the risk itself. As a rule of thumb however, we argue that the present differences in the use of joint calculations, mainly depend on market size, market concentration and historical background.

National markets with a low degree of concentration and smaller markets typically show considerable support among insurance companies to cooperate in joint calculations and tables. In some markets, few players are big enough to establish their own risk statistics. In others, the moderate size of the market itself may compel the bigger players to gather technical data together with smaller competitors.

In order to have high quality statistics regarding automobile accident assurance for example, a minimum number of observed cars and accidents is required. In smaller markets like the Belgian market, even the bigger players do not insure enough cars to build these statistics themselves. Cooperation is thus crucial. In highly concentrated markets of sufficient size on the contrary, one will typically find less support to participate in joint calculations. Dominant players will often have trustworthy internal data and will not easily be convinced to share them with competitors.

It is important to take into account the dynamics of the insurance market. Similar to other national insurance markets, the Belgian insurance market went through a consolidation process over the last decade, and has evolved to a certain degree of concentration. In some of the new member states however, market concentration is not the result of natural economic dynamics over time, but due to political history. Such a historically generated level of concentration may explain why the BER is not or less used in a number of new developing markets.

By providing a ‘safe harbour’ for joint calculations and tables, the BER has considerably contributed to the performance of the Belgian insurance market, to the benefit of consumers. Assuralia fears that this positive technical cooperation would be in peril if the BER would no longer provide legal security. We are convinced that starting up the accessible databases that exist at present would be more difficult in today’s market.

Reducing or abandoning joint calculations, tables and studies would have detrimental effect on market dynamics in general. As the cost of trustworthy data would increase, small players would in practice find it hard to follow the conditions and product design of the dominant players. Growth by innovation and actuarial quality would become the prerogative of the dominant players in the market.

From a supervisory point of view, Thomas Steffen from CEIOPS rightly recalled during the Hearing of 9th February 2007 that data used by insurers must be extensive in order to be reliable. Without such information, pricing, financial control, profit or loss and all the other fundamental commercial decisions, cannot be properly made. He rightly pointed out that the crucial Solvency II project encourages insurance companies to share technical data rather than the opposite. Smaller insurance companies do not always have these data available and must rely on aggregated market data.[4]

### *Pools*

Pools often exist because of the societal and political expectations regarding the insurance sector. Such expectations vary among member states and so do the pools or other systems of common coverage. The fact that they are rarely used in a number of states does not mean that they have no use in general. We believe that differences regarding the use of pools may well result from different roles of the public and private sector, on the one hand, and from public authorities' decisions or regulation, on the other hand. In practice, pools are very often created for high intensity risks and for legally compulsory insurance. They can be regarded as the expression of the insurers' commitment to specific risks, although within the limits of risk sharing.

In a number of areas with risks of high intensity, insurers cannot bear the costs alone as they may be too large for insurers or even for the market as a whole. Nuclear risks are for example in a number of member states shared between the state and the private insurance sector by means of a layered system. The insurance sector covers a part of the insured liability while state guarantees cover the rest. Similar solutions are developed for terrorism insurance and insurance for natural hazards such as flooding, with the participation of the State to share the risk. They show that sharing the risk among insurers provides viable and necessary insurance solutions for otherwise uninsurable risks, without hampering competition on the insurance market.

In many a Member state, national law obliges people to subscribe certain insurance products. Affiliation with third party liability motor insurance and with workmen's compensation insurance is for example obligatory in Belgium. Such systems necessarily require specific measures for people or enterprises that cannot or do not want to find insurance on the market. Pools and agreements to share exceptional risks are then often suitable solutions. They increase capacity to an extent that a market would not be able to achieve spontaneously.

## VI. Access to insurance

During the hearing on 9th February 2007, concerns were raised regarding the availability and affordability of business insurance cover for the professional risks of SMEs with cross-border operations. In this regard, one should certainly take into account the cyclical nature of the insurance market. In times of high profitability, insurance companies may well be more willing to engage in FOS operations than in a hardening market.

Problems with professional risk insurance for cross-border businesses are mainly due to the vast complexity of the legal and tax environment, however. Legal and tax systems, crucial aspects for the success of any insurance product, are predominantly shaped on the national level. In order to have affordable insurance for cross-border SME operations, Assuralia argues that considerable simplification efforts with regard to the legal and tax environment, both at the national and European level, are necessary.

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[4] Speech Thomas Steffen at the EU Commission Public Hearing on the Business Insurance Sector Inquiry, 9th February 2007.