CONVENIENCE TRANSLATION FROM GERMAN

Statement

on the Interim Report prepared by the EU Commission in relation to its Inquiry into the European Business Insurance Sector

Contents

Summary

The GDV welcomes the Interim Report presented by the EU Commission in relation to its Inquiry into the European business insurance sector. The Interim Report does not suggest any specific anti-competitive practices within the meaning of Articles 81 and 82 of the EC Treaty that might impede the creation of a single business insurance market. However, neither does it state the objective principal impediments that exist in relation to the creation of a single insurance market: The insurance sector, the product of which - unlike the sale of goods - is solely governed by legal arrangements, is more greatly affected than any other sectors by linguistic differences and differences in national rules on damages and liability as well as in insurance law, which pose an impediment to the creation of a fully integrated single market. Despite the fact that cross-border insurance transactions - in particular in the field of business insurance - will be difficult as a result of the aforementioned differences, the effects of these impediments can be softened by utilising the exemptions available under the Block Exemption Regulation for the Insurance Sector on a national level and, for instance, by providing new market entrants with claims expenditure statistics and sample insurance terms.

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Therefore, there is an urgent requirement for the maintenance of the Block Exemption Regulation for the Insurance Sector beyond 2010, in particular since the considerations under the current Block Exemption Regulation (Commission Regulation (EC) No. 358/2003) continue to apply. Under no circumstances should any conclusions be drawn with regard to the Block Exemption Regulation as a whole from a business insurance sector inquiry.

Claims expenditure statistics provide insurers with a secure base for their own tariffs with a high degree of statistical reliability and enable them to continue to develop that base. These statistics significantly contribute to the availability of a sufficient range of insurance types, and they also facilitate cross-border market entry. First and foremost, this secure tariff base enables insurers to ascertain their price limits and take new risks. Thus, claims expenditure statistics also promote competition within a market. It is striking when looking at the German market that concentration is especially low in those customer segments where valid and substantiated claims expenditure statistics are available.

Sample insurance terms constitute an orientation aid for insurers, policyholders and third parties alike and form a legally solid base for additional insurance cover. It is proven by numerous examples that sample terms for Germany neither pose an impediment to innovation nor that they result in a homogenisation of insurance products. Rather, they enable insurers to concentrate their resources on drafting their insurance cover provisions with a view to competition aspects.

With regard to the statements made and the questions posed by the Commission in its Interim Report, the following should be noted:

- The view expressed by the Commission in its Interim Report that business insurance is particularly profitable cannot be confirmed for the German market based on the existing long-term data. No factual statements regarding general profitability can be derived in this context from the data for a single financial year, or even several financial years, since this sector must be observed over a longer period of time due to the extreme likelihood of major claims and the resulting volatility of results. It becomes clear from the figures relating to the specific developments in commercial (SME) and industrial (LCC) property insurance that, when taking into account market cycles, only a small yield was attained in the German market.

- Neither can the Commission's view that the industrial segment is "cross-subsidised" by the commercial segment be confirmed for the German market against this background and based on the actual results realised in the commercial property insurance segment.

- So-called "best terms and conditions" clauses are mostly exempt under Art. 2 (1) and Art. 3 of Commission Regulation (EC) No. 2790/1999, insofar as they constitute a competitive restraint in the first place.

- Insurance contracts with businesses are normally concluded for a limited one-year term in Germany. Even if an automatic renewal is agreed – provided no party cancels the contract – this does not constitute a competitive restraint because it is a mutually accepted market practice in the German insurance sector to dispense with notice periods and to re-negotiate insurance contracts on an annual basis.

- A disclosure of commissions by intermediaries, not least due to the statutory rebating prohibition under German law, is not suitable to promote competition. Regardless thereof, a disclosure obligation must in no event be introduced for dependent intermediaries or in respect of direct sales, as business is procured for one insurer only and this is also known to the customer.

- The reason for the varying degrees of use of the exemptions available under the Block Exemption Regulation in the national markets particularly lies in the number of market participants and the scope of the statutory framework pertaining to the characteristics of insurance products. The higher the number of market participants and the less intervention by the legislator in relation to product characteristics, the more intensive the use of the aforesaid exemptions. The spread of co-insurance particularly depends on whether particularly high risks are to be insured that, for insurance and business policy reasons, cannot be borne by the insurer alone.

1. General Comments

The German Insurance Association (*Gesamtverband der Deutschen Versicherungswirtschaft*; "**GDV**") welcomes the Interim Report prepared by the Commission and its intention to enter into open discussions regarding the effects of the Block Exemption Regulation.

In conclusion, the Interim Report shows that, in the past, progress was made on the way to a single market for business insurance, but that full market integration could so far not be realised. The statements in that regard, however, require further comments. In addition, it becomes clear at least with regard to the German insurance market that there exists lively competition between insurance companies and that breaches of competition rules cannot be ascertained.

1.1 Progress on the Way to a Single Market

In the chapter on market integration, the Commission observes that cross-border insurance business is mainly carried out through foreign subsidiaries which had already been established in the relevant member state and a majority stake in which was then acquired. In general, this corresponds to our own findings. A large German insurer, however, went a step further when it merged with a foreign subsidiary last year, thereby taking on the legal form of a *societas europaea*. In doing so, it showed that it has come to regard itself as a European enterprise. In addition, especially with regard to the retail segment, it must be observed that some insurers are starting to engage in cross-border business by way of the free provision of services. By way of example, we would like to mention the Internet insurer that is planned by the Zurich Group and that is to operate on a pan-European level. From our point of view this is the starting point of a general development.

The Commission seems to adopt a sceptical stance in relation to market integration by way of acquiring foreign subsidiaries. It fears that product innovations will not be transferred to the newly developed markets if existing insurers are merely taken over. However, the Commission should take into account that the acquisition of foreign insurance companies is the most sensible option in many cases for business policy and management reasons. Otherwise, the considerable investment over a longer period of time into the creation of the necessary structures, the specific market know-how and the required awareness level might result in only a marginal market share. In addition, the new market participant faces the risk of negative selection if it is not familiar with the local market.

We are also unable to ascertain the extent to which product innovation would be hampered thereby. Following the integration of the acquired entity into the group structures, the management will attempt to eradicate inefficient procedures and structures, thereby improving production. This is also beneficial to policyholders. In addition, groups operating on a pan-European level, in the course of any subsequent integration, will monitor the insurance products on offer in the individual member states. This monitoring results in so-called "best practices", which means that products offered in one member state will subsequently also be introduced in the other member state by the relevant subsidiary. And this has exactly the effect envisaged by the Commission in connection with the cross-border provision of services.

Especially in the more recent past, however, cross-border market entries have also been taking place by way of the new incorporation of foreign subsidiaries or the provision of services.

Particularly in the German mass insurance market, more specifically in the area of motor insurance, there have been a number of successful market entries in the past few years that are characterised by a consistent increase in market shares. For instance, Direct Line, a UK provider of motor insurance, is a successful participant in the German motor insurance market and has been active in Germany since 2002. As stated in the company's 2005 annual report, which is available online, its gross premium revenue and insurance portfolio has been increasing by double-digit percentage figures since its starting year 2002. In comparison, the average growth of its German competitors has been in the lower single-digit percentage area. In 2006, the UK insurer Admiral followed suit and entered the German market directly.

The Commission also believes that full market integration will result in a balancing of member states' different insurance cycles. However, this will be true to a very limited extent only. This is because insurance cycles mainly come into existence when premiums are increased following years of particularly high losses. If, however, losses occur on a pan-European basis or European insurers are equally affected by global events such as the terror attacks of 11 September 2001 or grave natural disasters (storms, hurricanes or earthquakes in affluent areas), the insurance cycles within the EU will also be aligned with each other. Globally occurring external factors - such as the capital markets crisis that started in 2001 - can also have a significant impact on the start and/or course of an insurance cycle. In that case, there will be no differences in insurance cycles that could be balanced.

1.2 Reasons for Lack of Full Market Integration

The Commission initially correctly states that, from an insurer's perspective, the principal reasons for entering a foreign market are financial and commercial considerations.

Naturally, insurers - being profit-oriented businesses - will primarily invest in markets that promise significant growth and profit, which is not least due to the fact that the insurance business is connected with significant risks; in this context, particularly the long-tail risks pertaining to liability insurance should be mentioned. By contrast, if the necessary initial investment is very high in relation to the expected profits, insurance companies are unlikely to invest. Therefore, companies will always include the costs and risks of a market entry as a factors in their considerations. Market size can also be a relevant factor for an insurer when deciding whether to enter a foreign market or not. In absolute terms, a small market is likely to generate lower profits. If these lower profits also require a high initial investment, an activity in that market will probably not be worthwhile financially - unless there are special strategic interests.

The significant investment required for market entry is mainly determined by two factors that, at the same time, stand in the way of full market integration:

- **Differing national legal frameworks and risk environments**: Because of differing legal frameworks, the wording of an insurer's terms and conditions must be adapted to the rules of the relevant national jurisdiction, in particular the relevant laws pertaining to insurance contracts. In this regard, sample insurance terms are very helpful for foreign insurance companies. If no sample insurance terms are available, this will result in high initial investment for the drafting of new insurance terms, for which local lawyers might have to be brought in. On the other hand, differing national laws also result in differences in claims expenditure, which must be included in insurers' calculations. This particularly applies to liability insurance that covers the relevant statutory liability, but also, for instance, to business interruption insurance, since the national employment laws differ widely as regards mandatory payments to employees. For insurers without any experience in the relevant market, there is a danger of miscalculations, which is likely to prevent many insurers from entering a market. Only reasonable claims expenditure statistics within the meaning of Art. 1 lit. a of Commission Regulation (EC) No. 358/2003 will provide a foreign insurer with a sufficiently secure basis for its own calculations. Some "new entrants", for instance, have left the German insurance market again in the past because their business expectations did not come to fruition due to incorrect risk assessments. These companies include, for instance, the U.S. insurer Allstate, which had transacted business in Germany with a focus on motor insurance. Although Allstate did have GDV's claims expenditure statistics at its disposal, the company's product and tariff policy suggested that it was attempting to transfer the risk experience and know-how it had gained in the U.S. to the German motor insurance market and was thus unable to cope with the specific risks inherent in the German market. In terms of risk, the same vehicle type may have to be assessed in a completely different way in Germany and the U.S., for instance if a certain type of vehicle tends to be used by married couples with children in the U.S., but by learner-drivers in Germany. The same differences can also be of relevance within Europe.

- **Social and linguistic differences**: Due to the linguistic differences within Europe, a company's own insurance terms will at least have to be translated. As, however, the individual translated terms are likely to be interpreted in a different manner in the different national jurisdictions, a simple translation is generally insufficient; instead, new terms will normally have to be drafted, which incurs costs.

In conclusion, therefore, there are many reasons that prevent insurers from offering their products across borders - more than in the cross-border sale of goods. The effects of these impediments, however, can be softened if the insurance associations in the relevant national markets prepare and provide sufficient claims expenditure statistics and sample insurance terms. Then, a cross-border market presence will solely depend on profit expectations and business policy.

1.3 No Breaches of the Competition Rules Laid Down in Articles 81 and 82 of the EC Treaty

In several passages of its Interim Report, the Commission comes to the conclusion that it wishes further to assess the competition restraints caused by individual practices in the subsequent course of its sector inquiry.

In that regard, the general objective of a sector inquiry must be pointed out in advance. Pursuant to Art. 17 (1) s. 2 of Council Regulation (EC) No. 1/2003, the Commission may solely request the undertakings or associations of undertakings concerned to supply the information that is "necessary for giving effect to Articles 81 and 82 of the EC Treaty" and may carry out any inspections necessary for that purpose. This means that a suspected competition restraint or distortion must relate to such a restraint or distortion within the meaning of Art. 81 or 82 of the EC Treaty. Breaches of the competition rules laid down in Art. 81 and 82 of the EC Treaty, however, cannot be ascertained based on the results set out in the Interim Report:

- The **conclusion of long-term contracts** is not prohibited. Only in sample insurance terms pursuant to Art. 6 (1) lit. f of Commission Regulation (EC) No. 358/2003 long contract terms are not permissible. In addition, long contract terms can only be prohibited if they result in an abuse of a dominant position. However, at least with regard to the German market, constellations of that type need not be expected.

- **"Best terms and conditions" clauses** by which the user attempts to attain the most favourable terms agreed by other insurers for the (re-) insurance of the same risk with a policyholder are in most cases exempt under Art. 2 (1) and Art. 3 of Commission Regulation (EC) No. 2790/1999, insofar as they constitute a competitive restraint according to their intent and thus fall within the scope of Art. 81 of the EC Treaty.

- The Commission also mentions networks of insurance intermediaries that are bound by exclusivity agreements, as well as a previous inquiry which concluded that competition in Germany was not hampered by the high degree of **distribution via exclusive agents**. It must be noted in this context that the sale of insurance contracts via exclusive agents has declined further in Germany since the Commission's inquiry and now merely makes up for a market share of approx. 50%. In the area of business insurance, which is the subject-matter of the sector inquiry, the predominant sales channel in Germany is that of the insurance broker, which can also be used by foreign insurers. This is expressly mentioned on p. 93 of the Interim Report. In the area of business insurance, the significance of exclusive distribution declines in proportion to the customer’s size. The annual new entries by foreign insurers in Germany, in particular by way of establishing new branches, also show that a large portion of the sales channel using exclusive agents does not present an obstacle to cross-border market entries by insurance companies.

- The various **types of payment** to brokers and the lack of their disclosure do not breach competition rules. First, special services rendered by a broker on behalf of an insurance company (such as assisting in risk assessment or claims processing) must be remunerated separately; this does not constitute a competitive restraint. What is more, an insurance company must also be able to set its own business policy objectives, pursuant to which it might want to insure, in return for lower premiums, only those policyholders that tend to cause less damage, or it might want to insure, in return for relatively higher premiums, as many policyholders as possible without conducting a detailed risk assessment. This is what competition between insurers is all about and has so far been regarded as the special subject-matter of the secret competition between insurers. Commission payments to brokers that depend on certain factors, such as number or size or claims statistics of the brokered risks, and are thus coupled with "quality characteristics", are also merely a result of competition between insurers. Commissions of this type to brokers always depend on performance and do not prevent brokers from providing services to other insurers. A broker's obligation to find the most favourable offer for his customers of course remains unaffected. The dissolution of a potential conflict of interest on the part of a broker in his double function as a customer advisor and sales channel, however, is a matter under civil law and not competition law.

2. Issues Listed at the End of the Interim Report

Our responses to the specific questions posed by the Commission at the end of its Interim Report are as follows:

2.1 Discrepancy of Combined Ratios

Q.1 Are there compelling justifications for the apparent discrepancy in the level of combined ratios of SMEs and LCCs observed in some parts of the EU-25?

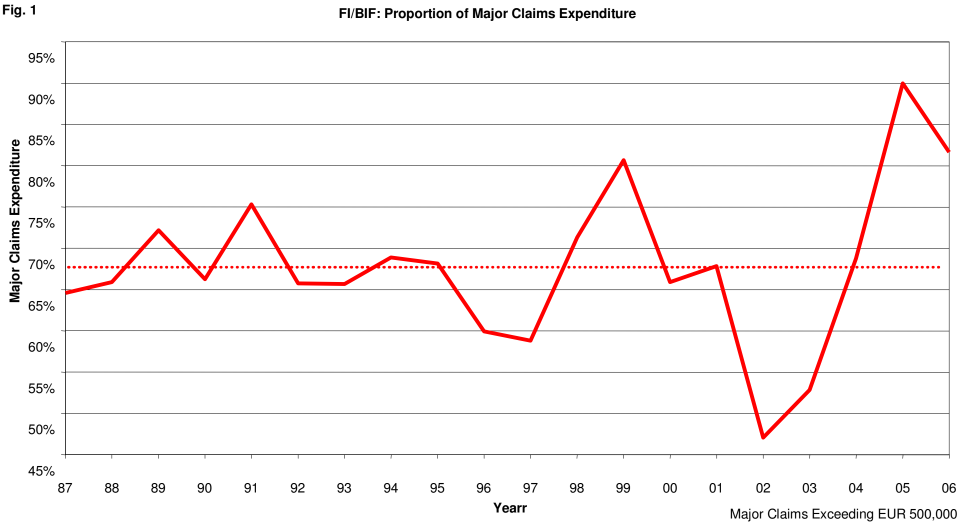
First, we would like to point out that there is no general threshold in the insurance sector in respect of defining policyholders as large corporate clients (LCCs) or small and medium-sized enterprises (SMEs). Allocation is made based on each insurer's individual criteria. The differentiation between SMEs and LCCs (for a definition, see pp. 152 and 154 of the Interim Report), which the sector inquiry uses as a basis and which serves different purposes entirely, is not reflected in the insurance sector's industry practice. For a differentiation as to insurance for LCCs and SMEs, other characteristics are relevant, in particular the turnover achieved by the enterprise to be insured; individual insurers, however, use different criteria in this regard. For instance, some insurers always allocate commercial risks to the LCC segment in the event of foreign permanent establishments or particularly serious special risks. Therefore, the figures used in the Interim Report concerning the individual customer segments are largely based on estimates rather than exact statistics.

Notwithstanding the foregoing, where figures can be rendered comparable, no general deviations in the combined ratios for LCC (industrial) and SME (commercial) insurance can be ascertained in the German insurance market that would support the hypothesis of a cross-subsidising benefiting the industrial segment. The following comments should be noted with regard to the Commission's findings set out in Section VI of the Interim Report (Financial Aspects):

a) No factual statements regarding general profitability can be derived in this context from the data for a single financial year, or even several financial years, since this business must be observed over a longer period of time due to the extreme likelihood of major claims and the resulting volatility of results. The volatility of results is also a major reason for the withdrawal of many insurers from the industrial business.

The effect of major claims, for instance in industrial property insurance, is illustrated by the chart below (Fig. 1). In industrial property insurance, major claims in excess of EUR 500,000 make up for 50% of total claims expenditure on a 10-year average; in the area of industrial fire insurance / insurance for business interruption due to fire (FI/BIF), major claims even amount to 67%; the total major claims expenditure in this context - as can be seen from Fig. 1 - fluctuates heavily. While, in the area of FI/BIF, the major claims expenditure in 2002 merely amounted to EUR 443.8m, it had risen to EUR 750m by 2005.

Fig. 1



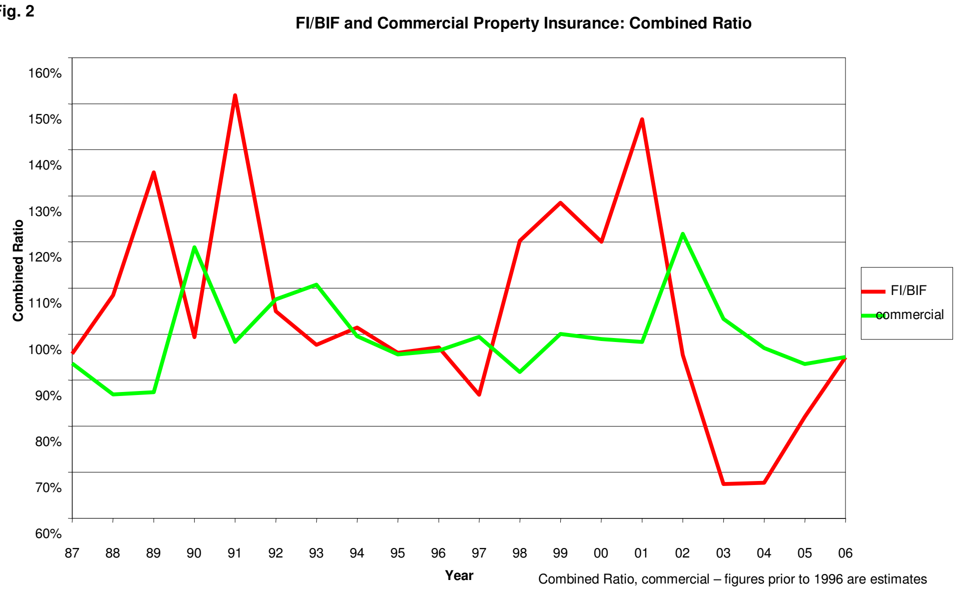
Naturally, in the area of industrial insurance, individual major claims have a greater effect on the combined ratio than in the area of commercial insurance, not least due to the lower number and the size of the insured risks. Accordingly, the calculations for industrial property insurance must be different from those for commercial insurance; this can lead to significantly more visible insurance cycles.

b) The statement by the Competition DG on p. 65 of the Interim Report, according to which the findings suggested that profitability was very high in business insurance, cannot be confirmed for the German market.

The only specific results available to the GDV in the context of business insurance relate to property insurance. Based on gross premiums received, however, industrial property insurance and commercial property insurance are also the largest segments, so that we will discuss property insurance below. With regard to the remaining insurance segments with a high proportion of industrial and commercial policies (such as general liability and transport insurance), by contrast, only aggregated total figures are available for all customer segments (retail/commercial/industrial).

As already discussed above, separate market figures are difficult to generate for the commercial and industrial segments, as there exists no defining market standard and, instead, each insurance company defines its own "threshold". Uniform definitions, which are also required for determining homogenous risk groups, are possible only based on the registered insured value in the context of the GDV's risk premium statistics. As these statistics, however, solely serve the determination of the market averages for claims frequency, average claims and claims expenditure, they do not allow for any conclusions as to the premiums, costs and profitability in relation to individual segments. Therefore, the chart below (Fig. 2), which shows the development of the technical results in relation to FI/BIF and commercial property insurance on the basis of the combined ratio and taking into account any potential winding-up profits, can only provide an "indication" as to the differing results in the two customer segments.

Fig. 2



When looking at the aforementioned results, the high volatility and cyclicity of the insurance-specific results is particularly striking. As a result of competitive behaviour, there is an alternation of "soft" and "hard" market phases. Their effects on the results situation are overlapped and thus strengthened or weakened by the random occurrence or lack of major claims. Thus, for instance, in a "soft" market, where results are already dissatisfactory for competition reasons, an unusually high major claims volume can result in an extreme, sudden deterioration of results. Phases characterised by insurance losses, however, can be "tolerated" for a limited time only by any insurer. If the "pain threshold" of insurance losses that are just about bearable has been reached for the majority of market participants, the "soft" market phase is followed by a phase of results consolidation. This process is in part further strengthened by other external factors, such as the performance of the capital markets. If, for instance, capital market yields fall during a "soft" market phase or if the insurer, as a result of a stock exchange crash, even has to expect losses from capital investments, the insurer will be under increasing pressure to implement corresponding consolidation measures. In this phase of a "hardening" market, extreme and sudden results improvements are possible, in particular if the premiums already received (e.g. for a year) are significantly above the expected claims level as a result of an unusually favourable claims development. For instance, this was the case in the FI/BIF segment in the years from 2002 to 2004, during which time claims expenditure was almost halved compared to 2001; in addition to the consolidation measures that had been instituted, this significantly accelerated an improvement in the results following the previous loss phase. Since 2005, however, the insurance results in this segment have been deteriorating significantly, so that the profit phase must be expected to be over by the end of this year.

If only the so-called "hard market" phase is observed within a market cycle, a completely distorted picture concerning profits in the insurance business emerges. Even though providers of industrial property insurance have been able to generate significant profits of EUR 1.29bn since 2002 in the current "hard market" phase, these are still offset by insurance losses of EUR 1.31bn stemming from the previous "soft market" phase from 1998 to 2001. The situation is similar in commercial property insurance: There as well, the total of the losses of EUR 590m accumulated in 2002 and 2003 still exceeds the cumulated insurance profits of merely EUR 370m since 2004. For the aforementioned overall period from 1987 to 2006, the balance of all insurance-related profits and losses in commercial property insurance amounts to a "red zero" and, in FI/BIF, even a loss of EUR 1.2bn. A reliable statement as to the volatility and cyclicity of the business can only be made on the basis of a period of at least 10 years.

The high volatility of the business results, particularly in FI/BIF, also results in significant business risks for this segment. Thus, a company will only be prepared to assume such a high business risk if it can expect corresponding yields in return. This is comparable to an investment in the share market, where high potential yields are offset by significant (loss) risks, while the conservative investment form of the savings account offers a high degree of certainty but also a relatively low yield potential. High yield expectations, on the other hand, mean that, based on unrestricted capital movements, international funding capital (e.g. Bermuda capacity) are quickly provided for the creation of additional insurance capacity, which is a development that can also be observed in industrial insurance in the "hard" market phases. Excessive and sudden upward changes in results are regularly dampened and/or quickly corrected by this.

In addition, it is a notable feature of the Interim Report that the combined ratios mentioned are particularly low in those segments that are either relatively new and thus still connected with a higher risk with regard to calculability (environmental liability, D&O insurance) or that show particular irregularities in their claims history (D&O insurance, aviation insurance). With regard to environmental insurance, the Commission's figures also clearly show that in this area, an increase in the combined ratio can be observed over time in contrast to the general trend. Thus, the so-called "innovation rent" is declining. Particularly high combined ratios, however, can be observed in those segments where knowledge of insurance risks and a high degree of data availability imply a lower risk, including from the insurer's point of view (general liability, motor insurance). Thus, the Commission's findings confirm that high combined ratios also depend to a very significant extent on high risk transparency and/or knowledge and a high degree of data availability for calculation purposes.

c) It should also be noted that the basis for the Commission's hypothesis regarding the profitability of business insurance was miscalculated. The Commission bases its findings on pre-tax profitability and defines this as 100, less the loss-expenses ratio, plus the ratio between net investment result and premiums. The Interim Report states a pre-tax profitability of 26%. This is based on the calculation of an average combined ratio in respect of business insurance for the whole of the EU for the year 2005. To this is added a figure for the net investment result, which was taken from a publication by Swiss Re. That publication by Swiss Re is quoted correctly insofar as it states a net investment result of approx. 16% of premiums. That publication, however, was published for a single occasion only and, in addition, solely states the net investment results for the years 1994 to 2004, and not that for 2005. It is inappropriate from an economic perspective, however, to make a connection between the net investment results for a period characterised by high investment results (and thus high loss and expense ratios) and a figure for another year in which investment results (and, consequently, the loss and expense ratios) were quite low.

d) The Commission's hypothesis that the commercial segment "cross-subsidises" the industrial segment cannot be confirmed either for the German market. This already ensues from the Interim Report itself which, on page 64, states a lower combined ratio for commercial insurance than for industrial insurance in Germany for the years 2000 and 2001, but a higher combined ratio for the years 2002 to 2005.

However, our own data as shown in Fig. 2 also show that there is no cross-subsidising in property insurance of the industrial segment by the commercial segment in Germany. Although, in the aforementioned overall period, the insurance-specific results for commercial property insurance, which correspond to a "red zero", are more favourable than those for FI/BIF, this is not related to any cross-subsidising, but is in part due to

- a greater claims likelihood in FI/BIF; and
- the fact that higher expected yields in the industrial segment quickly attract international funding capital, which evens out the potential yields.

When looking at the most recent market cycle, no significant differences in the profitability of the commercial and industrial segments are discernible anyway. The average combined ratio after settlement was rather similar in these two segments in the most recent market cycle: It was 101.9% in the commercial segment and 100.2% in the industrial segment.

In addition, cross-subsidising of one insurance sector by another within a multi-sector company would generally be unobjectionable under competition law:

As is recognised, the non-discrimination requirement pursuant to Art. 82 of the EC Treaty solely relates to circumstances that are comparable. There exists no obligation to treat all trading parties equally on a schematic basis. A discrimination applies only if all trading parties have been provided with "equivalent" services within the meaning of Art. 82 (2) lit. c of the EC Treaty but these equivalent transactions were subject to different terms. If the services are dissimilar or if there exist factual reasons for a differentiation, no discrimination applies. Therefore, if there exist other risks and other claims histories in industrial insurance than in commercial insurance, the insurer is well within its rights to charge different premiums. This possibility to differentiate factually is not overlapped by the objective of the EC Treaty to create a single market which is characterised by effective and genuine competition.

Cross-subsidising is also described by the Commission in other decisions as a procedure that is purely governed by business policy and that - particularly as a result of the methodical uncertainties in overhead costs allocation - can be found in any multi-product business. If an enterprise comprises profitable, less profitable and unprofitable business segments, the results of which are compensated in part or in full in the overall profit and loss account, this is regarded as being competition-neutral.

e) Finally, the alleged suspicion of cross-subsidising can already be invalidated by looking at the numbers of suppliers in both segments. In Germany, for example, the 91 companies engaged in the commercial property "mass business" comprise a mere 10 companies that insure top risks. Therefore, only these 10 companies (i.e. just under 11% of commercial suppliers) would theoretically be in a position to perform cross-subsidising of whatever kind. Thus, given the lack of a segment that allegedly requires cross-subsidising, the premium pricing of the remaining 81 companies is subject to purely competitive criteria. As a result of this comparably intense competition in the commercial segment, the remaining 10 industrial insurers are also unable to determine their relevant premium levels based on cross-subsidising criteria. Otherwise, they would no longer be competitive due to excessive premiums in the commercial business.

2.2 "Best Terms and Conditions" Clauses

Q.2 How widespread is the use of the so-called “best terms und conditions” clause in the reinsurance and in the co-insurance markets? Where does this type of clause originate?
Q.3 At what stage in negotiation does this type of clause appear and which/how many participants ask for its introduction?
Q.4 How is the clause enforced?
Q.5 What is the effect of this type of clause on the market?

The GDV has no specific information available as to how widespread the use of "best terms and conditions" clauses is, what types of these clauses exist and how many market participants use them. Neither has the GDV issued any corresponding non-binding sample clauses. Only as regards co-insurance has it become known from discussions with market participants that "best terms and conditions" clauses have no longer been applied for some years in that area. By way of supplement, we refer to our explanations set out in 1.3 above.

2.3 Long-Term Agreements

Q.6 Have you experienced that the duration of insurance contracts represented a barrier to entry for insurers wishing to penetrate new markets and/or acquire new costumers? Please explain your answer also taking into account the existence of termination and of automatic renewal/ extension clauses.

Q.7 Have you experienced that the duration of insurance contracts was a serious obstacle for switching to a different insurer? Please explain your answer also taking into account the existence of termination and of automatic renewal/ extension clauses.

According to our knowledge, insurance contracts are normally concluded for one year only in Germany, but they do often include an automatic renewal clause, which applies if none of the contracting parties gives prior notice of termination. This is beneficial to both parties, in that the entire contract does not have to be re-negotiated and re-concluded each year. At the same time, however, either party can abandon the contract if it thinks it will be able to enter into another contract on more favourable terms. This means that the insurer will terminate the contract if it thinks it can attain a higher premium or other, better terms. The policyholder will terminate the contract if it expects more favourable terms elsewhere. Thus, the renewal clause does not impede competition. Both contracting parties are able to seize better market opportunities and are not prevented from doing so by a long contractual term. Other insurers are not prevented from entering the market thereby.

In practice, the tacit renewal of a contract by another year is more of an exception in the industrial insurance segment. Instead, it is a mutually recognised market and contracting practice to waive notice periods and re-negotiate the insurance contracts each year, so that the policyholder is in a position to insure its risk with another insurer if it chooses to do so. For the policyholder, this has the advantage of a "safe haven" for its risk and that it is able to look for changed or new insurance cover with that added peace of mind. In addition to potential changes in the customer's risk structure, this market practice is mainly of significance to the insurer insofar as, in the global market, reinsurance contracts are only offered with terms of one year in each case. If prices were to rise or the scope of insurance were to be restricted in the reinsurance segment, the primary insurer would not be able to pass these changes on to its customers in the case of contracts with multi-year terms. Thus, the term of insurance contracts concluded with businesses does not exceed the required cover, so that there is no additional restriction on the scope of action of these businesses either.

Therefore, if a contract is concluded for a term exceeding one year, this almost exclusively results in advantages for the insured businesses: They secure a contract that is beneficial from their point of view for a longer period of time. Therefore, if the market is in a phase that is beneficial for the policyholder, customers will be increasingly interested in concluding multi-year contracts.

Thus, if the Commission, in its Interim Report, assumes an average contractual duration of just over two years in Germany, we interpret this to refer to the effective duration of the customer relationship rather than the contractual term agreed in each case.

2.4 Intermediaries' Remuneration

Q.8 To what extent do independent insurance intermediaries (brokers and multiple agents) disclose remuneration paid by insurers (i.e. commissions, contingent commissions including profit commissions, fees for services provided and other payments) to their insurance broking clients?

We have no reliable information available as to the extent to which independent insurance intermediaries disclose the commissions paid to them by insurers to their customers, but would like to refer to our statements contained in section 1.3 above in that regard.

However, a disclosure of intermediaries' remuneration, not least due to the statutory rebating prohibition under German law, is generally not suitable to promote competition.

If, however, the Commission should consider to oblige independent intermediaries to disclose the commissions paid to them, this must not apply to dependent intermediaries and direct sales in any event. With exclusive agents, conflicts of interest in relation to the procurement of insurance contracts as a result of differing commission amounts cannot apply because exclusive agents procure contracts for one insurance company only. This cannot lead to a distortion of competition as a result of differing commission amounts. In addition, it is known to the customer - at least in this scenario - that the intermediary is tied to one insurance group. As regards distribution costs of insurers using direct sales (e.g. via the Internet), it must be pointed out that distribution costs cannot be equated with commission/brokerage fee payments to intermediaries. Distribution costs normally also include other additional administrative and organisational costs that are incurred in any business.

2.5 Commission Rebating

Q.9 In your Member State, do independent insurance intermediaries rebate commissions to their clients? How common is this practice for SME clients? How common is it for LCCs?

Q.10 Are there any agreements between insurers and independent intermediaries not to rebate commissions to insurance broking clients? Are there any other practices that would discourage independent insurance intermediaries from rebating commissions to insurance broking clients?

In Germany, there has existed for many decades a rebating prohibition that was issued by the German Insurance Supervisory Authority and that is based on the German Insurance Supervisory Act (*Versicherungsaufsichtsgesetz*). It forms part of the prohibitions concerning special remuneration (*Sondervergütungen*) and contracts conferring special benefits (*Begünstigungsverträge*). The principal objective and/or sole motive of the supervisory authority as regards the prohibition of special remuneration was and is the **non-discrimination requirement** that is inherent in the insurance community. It is to be guaranteed that individual or groups of policyholders do not receive preferential treatment to the detriment of the remaining policyholders of an insurance company. Thus, the safeguarding of policyholders' interests includes keeping them free from unjustified burdens.

These motives have so far been decisive for all rebating and preferential treatment prohibitions and continue to apply.

In particular, these impositions by the supervisory authority safeguard the commission revenues of insurance intermediaries as well as the maintenance of the commission systems applied by insurance companies. An abolition of that prohibition would result in insurance intermediaries asking for higher commissions as a result of their reduced remuneration from insurance companies, even though some policyholders would profit from the rebating. Thus, there would be a danger that, as a result of higher commission charges, insurance cover for each individual policyholder would become more expensive, and a rebating would be effective only for those customers that receive it. This particularly shows that an increase in the price of insurance cover as a result of compensation claims by insurance intermediaries towards insurers concerns both the non-discrimination requirement in respect of policyholders and the protection of intermediaries' income, so that a rebating prohibition is required.

Neither did the ECJ raise any objections under competition law with regard to this prohibition in its judgment of 17 November 1993 in the "Meng" case (C-2/91). In addition, the Commission's guidelines regarding vertical competitive restraints (OJ C 291 of 13 October 2000, pp. 1 ff.) permit no-rebating agreements with so-called genuine commercial agents in the sense of paragraphs 12 to 20 of the guidelines, which apply to most insurance intermediaries in Germany. In Germany, insurance intermediaries are typically genuine commercial agents as they do not have to assume any financial or business policy risks from the activities carried out on behalf of the insurer.

We therefore assume that commissions are not passed on in Germany and that, accordingly, no special arrangements are in place between insurance companies and their intermediaries. Reference to the supervisory authority's requirements in respect of the rebating prohibition is made in the competition guidelines for the insurance sector, which are recognised by the German Federal Cartel Office (*Bundeskartellamt*) and which summarise the relevant German laws on unfair competition in relation to the procurement of insurance contracts.

2.6 Horizontal Cooperation

Q.11 The inquiry's data concerning the various forms of cooperation among insurers shows substantial differences among Member States. How can these differences be explained?

Q.12 Which sorts of benefits have you experienced, as a business insurance customer, from the forms of cooperation among insurers described in the present Report?

Q.13 As a business insurance customer, have you ever experienced that the forms of cooperation among insurers described in the present Report were hindering competition?

As the German Insurance Association, we would like to comment solely on Question 11; in paragraph 2.6.2, we also explain the reason why the Block Exemption Regulation for the

Insurance Sector is used to a quite significant extent in Germany. These comments are made principally against the background that the Commission, by way of its Interim Report, intends to initiate open discussions regarding the necessity of a Block Exemption Regulation for the Insurance Sector and that this discussion may not be held on the basis of an inquiry into the business insurance sector. Since the Block Exemption Regulation is particularly used in the retail and commercial mass segments, the findings from the Interim Report, which incidentally did not yield any results that question that regulation, may not be the sole base of discussion.

2.6.1 Different Utilisation of the Block Exemption Regulation in the Individual Member States

A different utilisation of the cooperation between insurance companies in the individual national markets that is exempt under Commission Regulation (EC) No. 358/2003 is normally based on reasons that ensue from the different structure and the different development stages of Member States' individual insurance markets. In particular the following aspects need to be mentioned:

- With regard to the calculations within the meaning of the Block Exemption Regulation, the Interim Report shows that there is a particular lack of joint statistics in relation to the insurance markets of the accession countries in central and eastern Europe. Since 1989, these markets have slowly developed from monopolised markets with one state-run primary insurer and reinsurer each into competitive markets with (until recently) an increasing number of insurance companies. Initially, these markets were still dominated by the previous monopoly holders, which also pooled most of the market knowledge. The market shares of these former monopoly holders, however, have shrunk considerably. These markets still show a significant degree of concentration (the market share of the five largest insurers in Poland and the Czech Republic, for instance, is 84%). Since then, however, insurance associations have come into existence, which, due to a lack of resources, were able to develop market statistics only gradually in line with the declining market shares of the former monopoly holders. The statistics from these countries normally relate to motor liability insurance, which, however, was only developed gradually in accordance with the standards of the more developed markets.

- From the perspective of domestic insurers, there is little need for sample insurance terms where large parts of the insurance terms are already provided for in the relevant laws (such as mandatory insurance laws) or, until quite recently, were still dictated by governmental bodies, or where only a small number of large providers operate in the market. In particular if there are former state-run monopoly holders - as is the case in most accession countries - the drafting of sample terms will be started only gradually following the establishment of insurance associations and an increasing number of market participants in these countries.

- Co-insurance will be agreed upon particularly often where major risks need to be insured, so as to achieve a broader risk diversification. Thus, co-insurance becomes particularly relevant in large markets with high value concentrations. In many cases, even large insurance companies are unable to underwrite the risks by themselves for insurance-specific and business policy reasons.

- A cooperation with regard to the drafting of safety guidelines will be required only where the effectiveness of safety devices is not already monitored in a reliable manner by state-run organisations or consumer associations, but where, for instance, homogenisation takes place solely by way of a cooperation of manufacturers. In smaller Member States that do not have their own manufacturers of safety devices, it will also be appropriate to make use of monitoring measures carried out by institutions in other Member States.

- It is striking with regard to claims settlement agreements that, so far, these do not exist in the smaller Member States and the accession countries. Particularly in the accession countries, however, it should only be a matter of time before these countries enter into their own agreements in order to facilitate claims settlement for the benefit of policyholders, thereby reducing the increased costs incurred by insurers in these countries that have been ascertained by the Commission.

- The Commission's findings, pursuant to which insurers in the eastern and central European accession countries work relatively cost-intensively, generating high profits while, at the same time, they make the least use of the block exemption in relation to the joint drafting of claims expenditure statistics and sample insurance terms and also do without claims sharing agreements, are equally striking. By contrast, the German market also makes the most intensive use out of all European states of the possibilities under the Block Exemption Regulation for the Insurance Sector, but is the least concentrated market exhibiting the most intense competition. This means that the intensive use of the possibilities under the Block Exemption Regulation for the Insurance Sector results in a significant increase in competition and, at the same time, more favourable premiums for consumers. The reasons for this are set out in the following section. Overall, this supports the assumption that, instead of creating legal uncertainty by dispensing with a Block Exemption Regulation, the Commission should support the joint drafting of claims expenditure statistics and sample insurance terms in order to improve competition.

2.6.2 Utilisation and the Need to Maintain the Block Exemption Regulation for the Insurance Sector

The GDV expressly favours a maintenance of the existing Commission Regulation (EC) No. 358/2003 beyond 2010 for the reasons formulated by the Commission itself and would like to substantiate its position with regard to the individual exemption spheres as follows:

2.6.2.1 Calculations

a) The GDV, on a non-binding basis, regularly provides its members with a large number of statistics and studies, which are to serve these members as a reliable basis for their own pricing and which are used by almost all of these members, large and small insurance providers alike. In that context, **studies** containing market-wide projections of future claims in one type of insurance (projection studies) serve as an orientation guide for insurers with a view to determining a commercially appropriate pricing level. They constitute a controlling instrument that helps insurers to estimate the balance sheet consequences of their business policy. The GDV's **claims expenditure statistics** describe the differences between different risk groups and help companies in their individual determination of a risk-appropriate pricing structure. Reliable findings as to the differences between different risk groups are of vital significance for any insurer, small or large, if it wishes to survive. An incorrect assessment of the appropriate pricing level (i.e. the level of premiums) can be rectified swiftly - if competitive pressures are left out of account. It is disproportionately more difficult, however, to adapt the pricing structure to the risk structure if there is a lack of risk know-how and a corresponding incorrect risk assessment because knowing the true risk differences is connected with a more or less high degree of uncertainty for all insurers. If an insurer, which is faced with competition and which has wrongly assessed the risks underwritten by it, is unable to adapt its pricing structure to the actual risk situation, it will be "selected out of the market" in the course of competition. This is evidenced by the example of the U.S. insurer Allstate mentioned in section 1.2 above. It seems that the company attempted to transfer its risk experience and know-how gained in the U.S. to the German motor insurance market and was thus unable to accommodate the specific risk situation prevalent in the German market.

Therefore, claims expenditure statistics enable insurers to base their own prices on a safe and solid footing. As association data are based on the data concerning the entire market, risk projections can be made with a very high degree of statistical reliability. According to the "law of the large number", statistical projections are the safer the more risk information is available. Given the high degree of differentiation of tariffs in Germany - and thus the large number of risk segments to be considered - no insurer in Germany has available sufficiently valid information regarding all segments. Even very large companies could only make risk statements by accepting a fairly high degree of uncertainty - provided that they solely rely on information pertaining to their own insurance portfolio. In addition, there are segments that are typically characterised by rare but very costly claims scenarios. With regard to those segments, no insurer will have available sufficient risk know-how by itself.

The claims expenditure statistics provided by the GDV are adapted by members to their own individual risk situation and supplemented by additional risk know-how that is solely available to the company in question; thus, these statistics form a basis for innovation. Thus, the number of the pricing characteristics used by the individual insurers in all insurance sectors clearly exceeds the risk characteristics explained and generally used in the GDV's statistics.

The experience gained in Germany also shows that an insurer will be prepared to provide its own risk information for market statistics only if such information no longer gives it a significant competitive advantage. Thus, for instance, the claims expenditure statistics relating to motor insurance are broken down according to the six most frequent risk characteristics. In addition, however, motor insurers in Germany apply a large number of additional tariff characteristics. This year, the GDV will include three additional characteristics that have become commonplace in the market in its motor insurance claims expenditure statistics. Insurers were only prepared to provide this information to the Association for use in its market statistics after almost the entire market is now using these characteristics in its pricing, meaning that they no longer offer a competitive advantage to individual insurers. Based on these market data, more reliable risk information can now be obtained, which is of additional benefit to all insurers. A secure pricing basis also creates the conditions for further innovation.

b) Claims expenditure statistics contribute significantly to the availability of a sufficient range of insurance products.

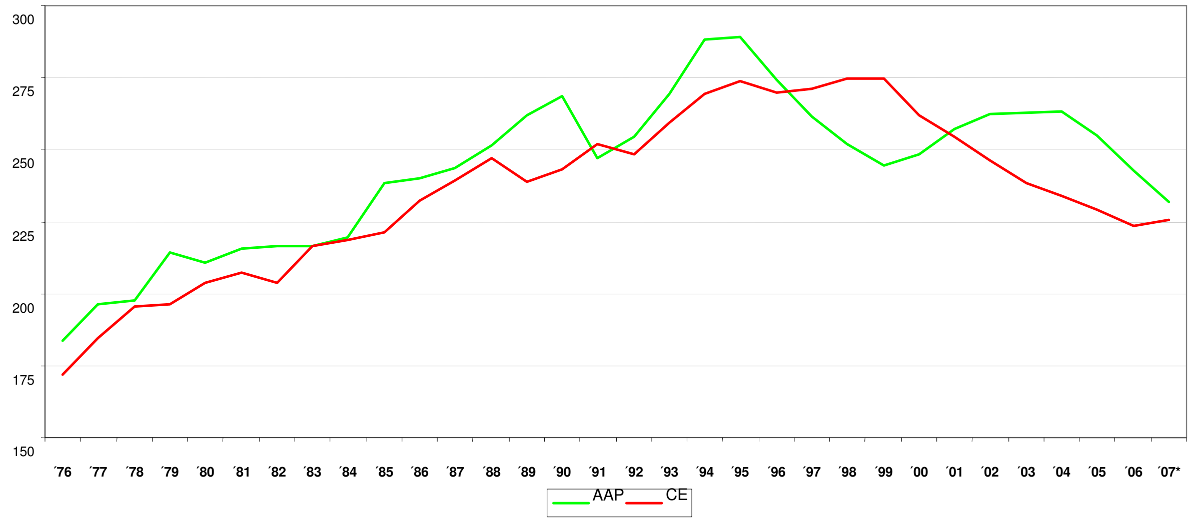
An insurer will offer insurance services in one business segment only if it has sufficient know-how pertaining to that business segment. In particular, this includes a correct assessment of the risks in that context. Thus, business segments in relation to which sufficient valid risk information is available offer a correspondingly varied range of insurance services. Claims expenditure statistics contribute significantly to this. This mainly applies to the retail lines in motor insurance as well as building and contents insurance, but also for the mass business of commercial property insurance (commercial and industrial) up to an insured value of EUR 50m, in relation to which the GDV provides valid claims expenditure statistics on a non-binding basis. If insurance groups are regarded as one supplier, then currently, for instance, there are 67 motor insurers, 96 building and contents insurers, 91 commercial and industrial commercial property insurers (up to an insured value of EUR 50m) in Germany, but only about 10 insurers in the so-called top risk business, for which reliable risk data pertaining to the whole market are not available.

As already detailed above, no insurer will be able to assess certain risks appropriately by reference to its own insurance portfolio. In the past, in Germany, these risks particularly included the so-called NatCat risks (natural catastrophes). Obtaining valid data in relation to these risks is almost impossible or connected with extraordinary costs for a single insurer. Only the joint obtaining and collating of market data via the GDV provided a solution to this problem. One typical example is "ZÜRS", the zoning system for floods, water backlogs and heavy rain (*Zonierungssystem für Überschwemmung, Rückstau und Starkregen*). Until the late 1990s, there was no valid assessment basis in relation to flood risks. This led the GDV to launch the ZÜRS project, establishing a geo-information system that allows for valid flood risk assessments. The storm and tempest insurance products on offer were only made possible by the introduction of this system; in other areas, the range of products on offer was expanded. The complexity of the tasks involved was and is so great that even leading insurers, in terms of logistics, would not have been able to implement, and maintain on a long-term basis, a system of that kind. In addition to the scientific challenges, this is also due to the fact that, in Germany, the individual states are responsible for flood protection. If the GDV had not developed the system, then indeed approximately 150 insurers would have had to negotiate with 16 federal states and an even higher number of government bodies in order to obtain data on floods. Only the collection of the relevant data by the GDV enabled the realisation of such a system in the first place and thereby made something available on the market that did not exist previously. Other countries (e.g. Austria, the Czech Republic, France) have meanwhile followed suit, copying the successful German approach. With the help of ZÜRS risk data, any insurer is now able appropriately to assess the likelihood of floods for all buildings insured in Germany. It has only become possible as a result of this information that, nowadays, practically all building insurers also offer storm and tempest cover.

c) Risk premium statistics, being a secure tariff base, make it easier for insurers to ascertain their price limits and take new risks.

It can be observed that, in segments where a high degree of pricing security is guaranteed by the availability of valid market statistics, insurers tend to adapt their pricing margins to the technical risk premium (claims expenditure/loss ratio) and tend to do with comparably small security margins. Valid risk data that are available for the entire market also support a large insurance capacity, which brings down prices by way of competition. The best example for this is motor insurance, in relation to which the GDV regularly provides its members with differentiated and comprehensive market statistics on a non-binding basis. As can be seen from Fig. 3, the premiums in the motor liability insurance segment are always close to, and sometimes even below, the technical risk premiums.

Fig. 3: **Average Annual Premium (AAP) vs. Claims Expenditure (CE) in Motor Liability (ML) (currency: Euro)**



If insurers have no or only insufficient information available as to a business segment's risk exposure, they will act more carefully in terms of their premium policy and include correspondingly high security surcharges in their premiums. This, for instance, should be the case in the new EU member states, where risk statistics for the entire market were previously unavailable.

The German insurance market, both in the retail, commercial and industrial mass business segments, is characterised by a large number of pricing characteristics, more of which are added on a continuous basis, especially in the retail segment. For policyholders, this means that premiums are increasingly and in an improved manner adapted to individual risks for their own benefit. Without the statistical certainty of a valid risk assessment basis, premium differentiation that is geared towards individual risk to such a high degree would not be thinkable. Therefore, certainty simultaneously creates a foundation for product innovation.

d) Claims expenditure statistics promote competition within a market.

The statement that claims expenditure statistics promote competition can be found in recital no 10) of Commission Regulation (EC) No. 358/2003, which is currently in force. That statement is still valid. If there is better knowledge and assessment of risks, a greater number of participants is possible in the market. The large insurance companies with high market shares can verify their own estimates; bigger benefits, however, ensue for small and medium-sized insurers. Their competitiveness is promoted. This was recently confirmed by the ECJ in its judgment of 23 November 2006 in the "Asnef-Equifax" case (C-238/05) concerning a Spanish credit agency. The ECJ states (at paragraph 55) that an exact risk assessment increases the effectiveness of an offer because the enterprise concerned is able to calculate the costs for its services more precisely and is not forced to apply high security surcharges. In addition, the ECJ states that improved knowledge increases customers' mobility as it was easier for them to change suppliers.

This assessment is confirmed by the market situation in Germany. It is striking that, in Germany, concentration is especially low in those customer segments where valid and substantiated claims expenditure statistics are available. This also holds true when the German market is compared with the markets of other EU member states. By contrast, there is only a small number of insurance providers wherever there is a lack of generally accessible risk information. For instance, as already explained, this applies to the top risk segment in industrial property insurance (above an insured value of EUR 50m) and industrial liability insurance (above a turnover sum of EUR 500m), which are not included in the GDV's risk statistics.

Contrary to the commercial and industrial "mass business", the preparation of market-wide claims expenditure statistics in relation to top risks is not necessarily desirable, as an appropriate assessment of top risks also requires very detailed and specific knowledge of the industrial customer to be insured, which is very difficult to reflect in market statistics. Companies that have available such specific risk data are understandably not prepared to share this competitive advantage with their competitors.

The finding that market statistics can promote competition has, in the United States, led to insurance companies being obliged under the McCarran-Ferguson Act of 1945 and the so-called rating laws of the individual federal states to provide their risk information pertaining to all relevant insurance segments for the preparation of market statistics to an institution admitted for that purpose (statistical agent), in order to enable any (potential) supplier to compete. In almost all federal states, that statistical agent is the Insurance Services Office (ISO), which is headquartered in Washington. Detailed information in this regard is available on the ISO's website at www.iso.com.

e) Foreign insurers that do business in, or intend to enter, the German insurance market also require claims expenditure statistics. For instance, all foreign insurers that have entered the German insurance market - whether by way of a takeover or cross-border market entry (these currently number 38 companies with a market share that has meanwhile risen to 20%) - have requested GDV statistics and now also contribute to them. The same applies to foreign insurers that intend to enter and compete in the German insurance market.

For instance, Direct Line, the aforementioned UK provider of motor insurance, is a successful participant in the German motor insurance market and has been active in Germany since 2002. Direct Line early on started to request claims expenditure statistics from the GDV and to participate in their drafting. We have been told by our contacts at Direct Line that, on the one hand, the company uses the know-how it has gained in the UK market and that, on the other hand, it also uses the claims expenditure statistics provided by the GDV in its risk assessment.

In addition, in Germany, there are a number of other foreign insurers that have entered the German insurance market not as a consequence of corporate takeovers but by way of external entry and that have used GDV claims expenditure statistics in that context. For instance, these also include AIOI Motor and General Insurance. The Japanese insurer AIOI is a subsidiary of the Japanese car manufacturer Toyota that distributes its policies via the Toyota dealership network.

f) It seems problematic to transfer assumptions that were made by reference to a different type of statistical work in the context of a business insurance survey to the mass business and to question the entire Block Exemption Regulation for the Insurance Sector for that reason.

The focus of insurance associations' statistical work lies on the retail segment and the commercial mass business. It is much easier to prepare valid market statistics according to the "law of the large number" for the mass insurance business than for business insurance. In the retail segment, it is relatively easy to determine homogenous risk groups by applying adequate actuarial procedures; in the business insurance segment, however, this is much more difficult because the required specific information is often not available. An accurate risk assessment in relation to business insurance generally requires specific know-how, e.g. in relation to a company's protective and security measures and its risk management quality, which are very hard to reflect in market statistics. Therefore, statements as to the value of business insurance statistics cannot be applied by analogy to the mass business.

2.6.2.2 Sample Insurance Terms

a) Non-binding sample insurance terms constitute an orientation aid for insurers, policyholders and third parties alike and form a legally solid base for additional insurance cover. In Germany, they have not resulted in a homogenisation of insurance products; this is also shown by the variety of products available, which is sometimes even lamented in published insurance reviews.

With regard to sample insurance terms, a differentiation must generally be made between descriptive clauses (i.e. clauses that describe the scope of the insurance cover) and non-descriptive clauses. Especially the latter are in many cases copied by insurance companies from the sample insurance terms drafted by the GDV. These are mainly provisions that are required under insurance contract law, such as termination options, provisions on breaches of duties, maturities etc. This saves all insurance companies costs they would otherwise incur for employees who would have to draft insurance terms 'from scratch' and follow the applicable legislation and practice of the courts in order to implement any necessary changes. The ongoing reform of the German Insurance Contract Law (*Versicherungsvertragsgesetz*) clarifies the complexity: For all classes of insurance the GDV has installed working groups with experts from member companies implementing the new legal framework in the sample insurance terms of the GDV, especially in terms of non-descriptive clauses. Further to ensure a high degree of legal certainty legal professors are employed as external consultants. This high degree of know-how bundling can only be achieved via the association.

Instead, when using available sample insurance terms, insurers can concentrate their limited resources on drafting deviating terms, in particular in the area of competition-relevant descriptive clauses, which set out the relevant insurance cover under these terms. The GDV's sample insurance terms always relate to a "median product line". They are neither an obstacle to, nor a driver of, innovation; instead, they are a "collection" of market data, which means that sample terms contain those descriptive clauses that have developed and established themselves in the market but have lost their competition-inducing powers. They then form the basis for additional innovative steps. This means that sample terms "lag behind" the market.

An example for the retail insurance segments is old-age accident insurance. In this segment, since 2003, insurance cover has developed in the German market in the form of so-called assistance services. In addition to the usual financial benefits, senior citizens who have sustained an accident receive assistance services that are designed to help them to remain in their familiar living surroundings. In the market, a large number of different services has emerged, e.g. daily food deliveries, cleaning services, etc. After old-age accident insurance established itself more and more in the market, the GDV drafted corresponding sample terms last year. Since then, the number of providers has risen significantly from just over 15 providers in 2005. Meanwhile, the market also goes beyond the mere senior citizen segment and also offers corresponding assistance services to families; for instance, in the event that the parent keeping the household has an accident, house-keeping services are provided.

The drafting of sample terms tends to be of greater benefit to smaller companies whose fixed costs would otherwise be as high as those of bigger companies but would have to be passed on to fewer insurance customers. Thus, smaller companies gain a greater degree of competitiveness in relation to bigger companies. In addition, smaller insurance companies would have difficulty developing their own insurance terms in the event of so-called new risks due to a lack of know-how and staff. For instance, the insurer that comes in 21st place in the property insurance market ranking only has a market share of just over 1%, which provides a clue as to its limited resources for activities of that type.

b) Also, in Germany, the courts play a major role regarding the particular question whether the relevant insurance terms are in compliance with the legal framework pertaining to general terms and conditions. It is difficult to remain up-to-date on that topic. Therefore, it is advantageous if sample insurance terms are jointly developed by several experts. In that case, there is a greater likelihood that the relevant clauses find the approval of the German courts, for instance concerning the clarity and completeness of the provisions. For the policyholder, this procedure has the advantage that it can generally rely on the effectiveness of the clauses and that the contract does not have to be amended during the contractual term. In particular, insurance companies do not have to implement any contractual adjustments (e.g. caused by a notice of termination pending a change of contract) because a clause has been declared invalid by a court and has therefore been deleted. If, however, such clauses are declared invalid in an individual case, it is possible to draft new clauses on short notice by combining the relevant expert know-how. The efforts required for the drafting of corresponding replacement clauses can be combined and accordingly implemented effectively.

c) Especially for the purposes of providing a sufficient range of insurance products with regard to newly occurring risks, the joint drafting of sample terms is required. This is confirmed by a current example pertaining to liability insurance:

In the area of liability insurance, insurance solutions are to be provided pursuant to the European Environmental Liability Directive (Directive 2004/35/EC of 21 April 2004) that provide comprehensive cover with regard to the newly introduced liability under public law. This particularly applies to biodiversity damage, a new claims category (damage to protected species and habitats). This is a completely new risk for insurers. In addition, the directive contains a large number of unclear legal terms, which will have to be explained in the insurance terms by reference to the directive. German insurers lack sufficient experience with insurance cover of this type because, so far, German employers' liability insurance has solely covered liability claims under civil law, while no cover existed for public law liability claims under these contracts.

According to the Environmental Liability Directive, safety systems (particularly insurance solutions) for financing the reversal of environmental damage will have been developed and be available on the European market as early as 2010. In that context, the Commission is even considering to decide upon an initiative for the introduction of European risk cover provisions after the year 2010.

Only if corresponding sample terms concerning the new environmental liability under public law are developed and distributed will a sufficient number of insurance companies be given the opportunity in the short term to gather information on this new risk and to offer customised cover for an estimated number of several millions of risks. The significant effort that was required for the drafting of these sample terms shows that probably only a small number of companies would have been able to develop corresponding insurance cover: For the development of non-binding sample insurance terms, a total of approx. 80 all-day sessions comprising various working groups of the GDV with a total of 25 experts from 12 different member companies were required.

d) New market entrants in the insurance business absolutely require sample insurance terms, in particular where a foreign language or a different jurisdiction is involved. Given the different national legal frameworks, a foreign company's own insurance terms cannot simply be translated and/or copied. Rather, the development of insurance terms requires knowledge of the relevant national laws and the jurisdiction implementing them. Therefore, insurance terms can only be drafted with the help of employees who are experienced legal experts with regard to the relevant jurisdictions. Taking this into account, it is simpler for a foreign company to use the sample terms provided by the relevant association and adapt them for its own purposes. This reduces the investment expenditure connected with the entry into a new market. It also lowers the market entry barrier. And this, in turn, has a positive effect on competition. The direct insurer Direct Line, which has been mentioned several times in this Statement, has also distributed its products from the start based on the insurance terms that were provided by the GDV on a non-binding basis.

Neither, however, do sample insurance terms present an obstacle to product innovation from abroad. In the area of motor insurance, this is evidenced by the fact that two companies have now introduced the "pay as you drive" insurance model, which is known from the UK market, into the German motor fleet business; under this model, the terms state that the motor insurance premium is based on the customer's actual driving behaviour.

In this context, D&O insurance must also be mentioned; this type of insurance was first introduced in Germany in the early 1990s by the German subsidiary of the U.S. insurer Chubb. After the first German insurers had started to offer D&O policies from around 1995, the GDV set up a working group in March 1996 for the drafting of sample terms, which were distributed on a non-binding basis in June 1997. Since then, an increasing number of German providers have included D&O insurance in their portfolios; we currently estimate this number at around 20 providers. The sample terms drafted by the GDV served many providers as a basis for their own drafts from which, however, they deviate significantly due to strong competition, in particular as regards the management's liability and excluded scenarios. While the original D&O policies were offered only with regard to the management of large public companies, they are now also offered for small and medium-sized companies.

e) For policyholders, sample insurance terms are of particular interest as a benchmarking tool in the retail segment. Policyholders can compare the terms offered to them with the sample terms of the relevant national association and determine whether they are favourable to them or not. However, sample insurance terms are used as a benchmarking tool to a greater degree by consumer protection organisations and rating agencies than by individual policyholders. They compare the details of the terms offered by insurers with the sample insurance terms and summarise the deviations in corresponding consumer journals that serve the forming of a public opinion. In this context, it becomes evident that, on the basis of the GDV's sample terms, such a diversity of products has evolved that product comparison is limited. This shows that sample insurance terms do not result in a homogenisation of products.

Potential policyholders can pre-select the appropriate insurance terms offered by the relevant insurers by studying the relevant journals. Thanks to this pre-selection, consumers can concentrate more on a price comparison and any other negotiation issues that are relevant to them. The only issue left to the consumer is how much he is willing to spend on additional risk cover. In turn, insurance companies are also forced into greater pricing competition.

f) For policyholders, sample insurance terms come with the added benefit that experts' comments on them will generally be available, which also contain extensive material on the legal practice of the courts in relation to their interpretation. Thus, it is easier for policyholders and/or their legal advisors to identify the benefits to which the policyholder is entitled. This often helps to prevent legal disputes concerning the scope of claims.

And finally, it is easier for consumer associations to take action concerning clauses they deem legally dubious. Currently, they merely have to bring a legal action in relation to a clause and possibly support/accompany all stages of appeal up to the German Federal High Court of Justice. However, they need not support/accompany actions in relation to a large number of clauses, the wording of which might only differ slightly. It is normally sufficient that a clause is declared incompatible once with consumer protection laws by a higher court. Consequently, consumers will then in most cases be able to refer to that decision. The fact that only few court proceedings are required in relation to a sample terms clause provides policyholders with a significantly increased degree of legal certainty.

2.6.2.3 Co-Insurance

a) The by far most common reason for the creation of co-insurance solution is the wish of the customer and/or his agent. In our estimation, the initiative for the creation of co-insurance in 93% of the cases originates from the policyholder's agent, in 2% from the policyholder himself and in only 5% from an insurer.

The decisive factor for the desire to set up a co-insurance community or even individual co-insurance is, on the one hand, the desire to maintain several liable parties wherever possible and, on the other hand, the option for brokers, which is mostly available, to negotiate better terms for customers.

b) Co-insurance solutions are generally suitable for covering major risks that individual companies cannot, or do not wish to, underwrite alone due to a lack of sufficient capacity. In that context, limited capacity can result from legal, operational or business policy reasons. From a legal perspective, the capacity of an insurance company is limited by the solvency provisions of the 1st and 3rd generations of European insurance directives as, in the event of major risks, the equity needed under the solvency requirements might not be available. However, a company's capacity is also limited for operational reasons. In particular, the assumption of a major risk must not jeopardise the existence of the insurance company as such or even limit its competitiveness. Thus, for instance, the realisation of an underwritten major risk might use up most of the equity or even put the company into a less favourable competitive position in relation to others. On the other hand, the (joint) assumption of many risks results in a better risk adjustment for individual insurance companies in accordance with the "law of the large number". Thus, co-insurance, as an alternative to risk diversification, becomes another option to and/or supplements re-insurance.

c) As regards certain less frequently occurring risks, particularly small and medium-sized insurance companies lack the knowledge that is required in order to be able to assess the risk properly and, where appropriate, correctly fulfil the contract in the event of a claim. This will particularly be the case where no differentiated claims expenditure statistics are available. By participating in a co-insurance community, small and medium-sized companies are enabled to gain experience with risks with which they were previously unfamiliar. However, this requires these companies to incur considerable expense because smaller companies, not least for cost reasons, cannot hire staff at their discretion for the assessment of, and claims processing in relation to, specific risks and because larger insurance companies will not pass on their know-how for competition reasons alone. However, smaller companies are thus always in a position to participate in the liability and premiums on a pro rata basis.

2.6.2.4 Security Precautions

a) Security precautions are of extreme importance for insurance companies: They contribute significantly to the reduction of a given risk and/or the prevention of losses or to being able to insure, or render insurable, risks in return for reasonable premiums, e.g. through the use of sprinklers, fire alarms or burglary/theft alarms. For the purposes of their risk assessment, insurance companies must know whether and to what extent these facilities actually reduce the relevant risk and prevent losses. Only if these facilities actually result in a significant risk reduction can insurers subsequently grant a reduction to their policyholders in the premiums payable. For that purpose, however, both the products and the facilities installed must have been tested as to their suitability. The same applies to the monitoring of the installation and maintenance companies, which is carried out in accordance with relevant guidelines. As long as these tests are not carried out in any meaningful manner by institutions that are independent from the manufacturers, such as government bodies or consumer protection organisations, insurance companies have to carry out these tests themselves.

b) The creation of technical specifications and guidelines regarding security precautions and their monitoring is also beneficial for consumers. Insurance companies and consumers share the same interests insofar as they want to know whether the facilities aimed at reducing risk are actually in functioning condition. Otherwise, insurers would grant unjustified premium discounts that would in the end have to be financed by all policyholders together, and consumers would be investing in malfunctioning security devices. This way, consumers receive an unambiguous, risk-specific framework from their insurer and are able to orientate themselves better in the complex area of assessing these facilities and the installation and maintenance company to be commissioned. On the consumers' part, this is mostly combined with the expectation that tested facilities will be accepted by all insurers.

c) Of course, individual insurance companies can carry out tests in relation to security measures themselves. This, however, would result in a disadvantage for manufacturers and installation companies, meaning that their products and/or companies would require not only one test, but possibly a separate test by each insurer. Consumers, on the other hand, would have no uniform orientation framework and would have to expect that a security device, once installed, would no longer be accepted by a new insurer. Consistent tests of security devices thus facilitate insurer changes, thereby promoting competition.

2.6.2.5 Claims Settlement

a) In the various European insurance markets, there is also a significant need for claims settlement agreements. Such a need regularly arises where several insurers are involved in a claim, whether they be private insurance companies and a national insurance carrier, two liability insurers in the event of shared responsibility in an accident or one property insurer and one liability insurer. In this context, claims sharing agreements bring significant benefits to all parties involved due to their generalised liability and recourse quotas that are customised to the most frequent scenarios.

The injured party can be compensated quickly. It does not run the risk of having to suffer disputes as to which insurer is liable for the damages or the amount of the proportion of liability, or of its insurer referring it to the other insurer. Rather, it is normally provided that the insurer which is first approached in relation to the claim pay up and settle the proportion of the damages not to be borne by it directly with the other insurer. In certain cases (particularly traffic accidents involving a large number of parties), it would also be extremely difficult to determine the exact proportion of liability in circumstances that cannot be completely clarified.

Sharing agreements allow insurance companies an effective settlement of damages, using state-of-the-art means of communication; sometimes, the settlement of damages is even automated. In addition, the large number of claims and the fact that each possible scenario can practically affect any insurer mean that, in the end, there is a fair distribution between insurers. The main advantage for insurance companies, however, is the immense savings of administrative costs that would otherwise be incurred if the amount of the share to be borne by the individual insurance company would have to be legally clarified initially by bringing in experts, lawyers and courts. The administrative costs incurred, which, not least due to the existing competition, are generally already fully passed on in the form of lowered premiums to policyholders, are becoming lower as a result of claims sharing agreements. Also, the injured parties do not need to go to court and, thus, receive their claims settlement more quickly.

b) In addition, claims settlement agreements must also be possible between insurance companies and the parties removing the damage, such as experts and repair workshops. Otherwise, injured parties who have a compensation entitlement against an insurer tend to follow the pricing structures of the parties removing the damage, even if they are completely exaggerated, as they themselves have no direct interest in low prices. In this context, insurers can ensure by way of agreements with the parties removing the damage that these do not charge excessive prices for damage removal, but instead the same prices they would charge parties who do not have a compensation entitlement against an insurer. Thus, pricing competition is reinstituted only in the context of the removal of damage on behalf of injured parties. This means that insurers' costs are lowered and the premiums for all policyholders kept low. Insofar as, however, the injured party is legally obliged to keep the damage to a minimum (damage/loss minimisation obligation), claims settlement agreements between an insurance company and a party removing the damage ensure that no dispute emerges at a later time regarding the damages and that the injured party quickly receives its compensation without having to go to court.

c) Therefore, claims sharing and settlement agreements should be block-exempt also in future, insofar as the Commission feels that they restrict competition in any meaningful way at all.

2.6.2.6 Legal Certainty

The aforementioned scenarios, which are currently block-exempt, would still be exempt pursuant to Art. 81 (3) of the EC Treaty without a Block Exemption Regulation for the Insurance Sector as they meet the exemption requirements set out therein and, in particular, also come with the mentioned benefits for consumers.

The fact that these scenarios "can be regarded as normally satisfying the conditions laid down in Article 81(3) of the Treaty", was also expressly stated by the Commission in recital 7 of Commission Regulation (EC) No 358/2003. There is no reason to assume that this statement no longer applies. However, without the Block Exemption Regulation, there would be increased legal uncertainty. As is known, a Block Exemption Regulation has clarifying character, meaning that any agreements that meet the requirements of the Block Exemption Regulation are exempt *ipso jure*. This is laid down with binding character for the courts and competition authorities. By cancelling the Block Exemption Regulation for the Insurance Sector, this legal certainty would no longer apply, and the Commission, by such cancellation, could not change the requirements laid down in Article 81(3) of the EC Treaty, which are the sole criteria for exemption.

Given the competition-promoting effect of the existing Block Exemption Regulation for the Insurance Sector and the legal uncertainty that might arise without it, there is a definite need for a successor regulation to Commission Regulation (EC) No 358/2003 beyond 2010, in particular also against the background of the special properties of the insurance product, which exclusively consists of a legal agreement and the costs of which can due to the uncertainty of potential claims only be calculated with a high degree of certainty on the basis of safe and solid data concerning the entire market.

Berlin, 10 April 2007