Status and Prospects for EU Legislative and Policy Initiatives in the (Re)insurance Sector

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INTRODUCTION

The European insurance industry is the largest in the world[1], with a 35% share of the global market in 2014. Insurance Europe, the European insurance federation, reports that its members invest over €8 500bn in the economy. French, German and UK insurers hold the largest share of investments, with a significant proportion held in government and corporate bonds.

Over 5000 insurance companies, of which 30 are large groups, operate in Europe[2]. Of the nine insurers identified by the International Association of Insurance Supervisors (IAIS) as Globally Systemically Important Insurers (G-SIIs), five are EU-domiciled: Allianz, Aviva, Axa, Generali and Prudential plc. Together they directly employ nearly one million individuals. As many outsourced employees and independent intermediaries[3] work in the sector. Bancassurance is the main life distribution channel in many European countries, whereas sales of non-life policies are dominated by agents and brokers[4].

EIOPA[5] reported in December that positive market sentiment had contributed to increased stability in the large EU insurance companies. As of October 2014 over 80% of the top 30 European insurance companies had a stable outlook. However, EIOPA warned that the weak macroeconomic environment, the risk of a prolonged low yield environment and credit risk would present challenges to European (re)insurers this year[6].

The sections below describe some of the main EU legal and policy developments of interest to the (re)insurance sector. In view of the complex reform in the EU of the financial sector following the financial crisis and given the continuing difficulties in achieving political consensus at the EU level, they do not claim to be exhaustive.

REGULATION

Sources and Territorial Scope

Currently more than 14 separate EU Directives are the principal sources of EU insurance and reinsurance law. The Solvency II Directive, which will apply throughout the EU (and the EEA[7]) from 1 January 2016, will codify much, but not all, relevant legislation. In addition, national legislation will continue to apply in important areas.

Switzerland is not part of the EEA. Relations between the EU and Switzerland are underpinned by a series of bilateral agreements. A 1989 bilateral agreement on non-life insurance facilitates establishment in the EU through branches. However, Switzerland is not otherwise subject to EU (re)insurance law and Swiss insurers do not enjoy any market access rights to conduct business within the EU on a direct cross-border basis. Switzerland is a candidate for equivalence[8] under Solvency II.

Taking up insurance and reinsurance activities in the EEA is subject to prior authorisation. The conditions and procedure for authorisation are harmonised under EU law, but the authorisation itself is granted by the supervisory authority of the home Member State[9].

Insurance and reinsurance undertakings authorised in their home Member State may carry on their activities throughout the EU by establishing branches on the territory of another Member State or by providing services on a cross-border basis[10].

Although EU law promotes cross-border operations, undertakings must still comply with extensive EU and national law safeguards regarding retail product offerings and consumer protection (where applicable and often referred to as "general good")[11].

[1] Statistics No. 50 European Insurance in Figures, 6 Jan 2015, *Insurance Europe*. Figures are based on yearly data collected by member associations and other organisations. Swiss Re, for instance, is the source for data on worldwide premiums. "Europe" includes Russia and Ukraine (which together account for less than 1% of worldwide premiums).
[2] *Insurance Europe*.
[3] *Insurance Europe*.
[4] *Insurance Europe*.
[5] *i.e.* the European Insurance and Occupational Pensions Authority, one of the three European Supervisory Authorities described below.
[6] EIOPA Financial Stability Report | December 2014.
[7] The EEA (European Economic Area) comprises the 28 EU Member States, Iceland, Liechtenstein and Norway.
[8] *i.e.* recognition by the EU that its insurance supervisory regime is equivalent to the Solvency II regime.
[9] See, for example, Title 1, Solvency II Directive.
[10] See, for example, Chapter VIII, Solvency II Directive.
[11] In 2000, the European Commission set out criteria for determining whether Member State general good rules conform to EU law in an Interpretative Communication, which also includes useful examples.

Regulatory Developments

The European Commission first proposed a Directive for an up-to-date solvency regime – Solvency II – in the summer of 2007, followed by an amended proposal in February 2008[12]. The Solvency II Directive was adopted in November 2009[13], with its entry into force scheduled for 1 November 2012.

In January 2011, the Commission proposed a revision to the Directive (known as Omnibus II)[14]. Omnibus II proposed amendments to certain areas of Solvency II such as:

- The implementation date;
- Transitional arrangements; and
- The form and basis of implementing measures, based on the 2009 Lisbon Treaty.

Changes were also necessary to reflect the establishment of the new European financial supervisory architecture (see below), and certain concerns following the financial crisis, in particular the treatment in Solvency II of long-term guaranteed products.

The Omnibus II proposal was subject to protracted negotiation between the Parliament and Council. The completed Directive was published in the Official Journal on 22 May 2014. Thanks to additional legislation, which was passed in the interim (the so-called "Quick-fixes" I and II), the Solvency II Directive will now apply from 1 January 2016.

Solvency II is a framework directive: this means that, following technical advice from EIOPA[15], the Commission must adopt detailed rules in a series of "delegated acts" or "implementing acts" which cover more than 40 separate areas of the Framework Directive. The first Solvency II Implementing Technical Standards (ITS) and Guidelines have been adopted. For the ITS, these concern "approval processes"; and for the guidelines, they cover "approval processes, including Pillar 1 (quantitative basis), and internal models".

EIOPA is currently conducting public consultation on the second set of ITS and its accompanying guidelines. They cover Pillar 1 (quantitative basis), Pillar 2 (qualitative requirements), Pillar 3 (enhanced reporting and disclosure) and supervisory transparency. The advice will be sent by 30 June so that the Commission may prepare and adopt the ITS delegated acts in time for the Solvency II start date on 1 January 2016. The second set of guidelines will be published by EIOPA in July 2015.

Insurance Regulation: Operators and Instruments

The Commission initiates EU legislative proposals. They are generally adopted using the "ordinary legislative procedure[16]". This requires agreement between the two co-legislators, the Parliament (751 Members) and Council (the 28 EU Member States).

For the past 10 years, as financial services legislation has become ever more complex, and, therefore, more difficult to negotiate, a four-level approach has been developed, known as the Lamfalussy process (named after the chair of the advisory committee which initially created it). Thus, framework legislation (level 1), usually a directive (such as the Solvency II Directive) or a regulation, is adopted setting out the main legal provisions and identifying areas for delegated acts (level 2). These are developed and adopted by the Commission in the form of directives, regulations or decisions, or technical standards (level 2.5), developed by EIOPA and adopted by the Commission by means of delegated or implementing acts in the form of Commission regulations or decisions. Level 3 covers non-legally binding guidelines and recommendations issued by EIOPA to ensure consistent implementation and cooperation between the supervisory authorities. Level 4 covers compliance and enforcement, including through the Court of Justice of the European Union (CJEU). As a result in particular of the financial crisis, both banking and insurance will be subject to more granular capital/solvency requirements in the years to come. As summarised below, standard-setting and supervisory oversight across financial markets are also more developed than before the crisis.

[12] *i.e.* "*Amended Proposal for a Directive of the European Parliament and of the Council on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II)*". Available at: http://ec.europa.eu/internal_market/insurance/docs/solvency/proposal_en.pdf

[13] Available at: http://eur-lex.europa.eu/JOHtml.do?uri=OJ:L:2009:335:SOM:EN:HTML

[14] *i.e.* "*Proposal for a Directive of the European Parliament and of the Council amending Directives 2003/71/EC and 2009/138/EC in respect of the powers of the European Insurance and Occupational Pensions Authority and the European Securities and Markets Authority (Omnibus II)*". Available at: http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:52011PC0008:EN:NOT

[15] *i.e.* the European Insurance and Occupational Pensions Authority, one of the three European Supervisory Authorities described below.

[16] Article 294, Treaty on the Functioning of the European Union.

The European System of Financial Supervision

Following the work of the De Larosière group in 2009, three independent European Supervisory Authorities (ESA) came into operation in 2011:

- The European Banking Authority (EBA);
- EIOPA; and
- The European Securities and Markets Authority (ESMA).

Together with the European Systemic Risk Board (ESRB), which oversees risk in the financial system as a whole, and the Member State competent authorities, they comprise the European System of Financial Supervision (ESFS). This was complemented in autumn 2014 by enhanced bank supervision, led by the European Central Bank (ECB), as part of European Banking Union (there are currently no plans to extend ECB direct supervision to insurers and reinsurers).

The incoming Commissioner for Financial Stability, Financial Services and Capital Markets Union, Jonathan Hill, must conduct a review of the ESFS and legislative proposals may follow. In particular, Lord Hill has been instructed to "*review the governance and the financing of these Agencies. On the latter, you should find a way to eliminate EU and national budgetary contributions to the ESAs which should be wholly financed by the sectors they supervise*"[17]. EIOPA Chairman, Gabriel Bernardino, has called for EIOPA to have an "*enhanced supervisory role for the largest important cross-border insurance groups*" in the medium term. Leading Members of the European Parliament share his view[18].

New Instruments

The ESAs have been described as "*some of the most powerful autonomous institutions ever established at EU level*[19]" and for good reason: not only do they contribute to the legislative process by, *inter alia*, advising the Commission on draft level 1 legislation, they also play a key role in the development of "technical standards". These comprise Regulatory Technical Standards, which in effect harmonise key provisions of EU law, and Implementing Technical Standards, which are to be applied in the Member States[20].

Of the three ESAs, EIOPA is the most relevant for insurers and reinsurers, although given the interconnectedness of financial markets, the work of the others may apply, depending on the subject matter. Its mission is to: promote sound regulatory supervision; avoid regulatory arbitrage; and protect consumers.

All three ESAs may develop technical standards, which apply to operators. They may also develop guidelines and recommendations for national supervisors (on a "comply or explain" basis). They have a mediation function to settle disputes, a role in crisis management, and a duty to monitor market activity. The ESAs also jointly run a Board of Appeal to protect the rights of parties affected by decisions adopted by the ESAs (see below).

Third Country Insurers

Not all EEA Member States permit non-admitted insurers to cover risks in their territory. Some restrict activity according to business lines. This is not expected to change with Solvency II.

Third-country undertakings with significant operations in the European insurance market and European undertakings with substantial non-EU business have, however, monitored closely developments under Solvency II. The equivalence process has been a particular focus, because of the promise of significant benefits for such firms, depending on whether their home jurisdictions are deemed "equivalent" by the Commission.

Third countries are encouraged to seek "equivalence" – a verification procedure to determine whether the third country's legislation and supervisory practices are broadly equivalent to Solvency II.[21]

Switzerland is the only third-country jurisdiction to have applied for the full equivalence procedure. Japan has only applied for reinsurance and Bermuda is only seeking equivalence for its commercial insurance sector, not its captives. Other countries have expressed interest in a "temporary equivalence" regime, a process introduced under Omnibus II[22]; still others prefer doing so on their own terms (*e.g.* the USA[23]).

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[17] Mission Letter from Commission President, Jean-Claude Juncker, November 2014.

[18] See European Parliament resolution of 11 March 2014 with recommendations to the Commission on the European System of Financial Supervision (ESFS) Review drafted by German Green MEP, Sven Giegold.

[19] Everson, Michelle. 'A Technology of Expertise: EU Financial Services Agencies' LEQS Paper No. 49/2012.

[20] In accordance with the "Meroni doctrine", final competence and accountability rests with the European Commission, but in practice the ESAs provide a great deal of technical expertise and drafting input.

[21] See Articles of the Directive: Articles 172 on reinsurance, 227 on EEA group solvency calculation and 260 on group supervision of EEA insurers with parents outside the EEA.

[22] http://ec.europa.eu/internal_market/insurance/docs/solvency/letter201202_en.pdf

[23] The EU-US Insurance Regulatory Dialogue Project.

Concerns that EU insurance groups would have to hold much more group capital to compensate for potentially lower requirements in the third countries in which they operate led to a last-minute deal in the Omnibus II negotiation, at the Parliament's initiative, to introduce an additional form of equivalence. "Provisional equivalence" will be available for 10 years, renewable for further periods of 10 years, where the criteria continue to be met.

Further work is needed before the final equivalence framework is complete, and no final decisions on the candidate jurisdictions have yet been made. For first wave candidate countries for full equivalence, EIOPA recently updated its advice to the Commission on their progress and held a public consultation. IAIS standards scheduled for 2019 will complete the picture.

Position of Brokers

The 2002 Insurance Mediation Directive (IMD[24]) sets out minimum standards for (re)insurance intermediaries and (re)insurance mediation/conduct of business. It does not currently cover direct sales.

Intermediaries must register with a competent authority in their home Member State, meet that authority's professional requirements, and notify it of any intention to establish or provide services in other Member States. The IMD also specifies certain pre-contractual and contractual information the intermediary must provide and the form in which this must be provided to the customer.

The IMD includes basic provisions on sanctions, complaints-handling, and other redress mechanisms. Cooperation arrangements between the Member State competent authorities are set out in the IMD, but have been subsequently supplemented by an EIOPA text, the Luxembourg Protocol.

Review of the IMD (IMD 2)

The IMD is being reviewed. The Commission would bring direct sales forces within its scope, as well as claims management and loss adjusting (although the Parliament would exclude the latter). Special information requirements are proposed where suppliers "bundle" products together, and restrictions are expected on product "tying". The chapters on professional qualifications, as well as administrative sanctions and penalties, will also be revised.

[24] Available at: http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:32002L0092:EN:HTML

Disclosures for retail investment products

A central theme in the review is management of conflicts of interest, in particular through disclosure of remuneration, and is linked to a wider initiative designed to review the sales process for sales of retail investment products.

The key text in this regard is the recently adopted revised Markets in Financial Instruments Directive (MiFID II). Sales of insurance investment products such as unit-linked and "traditional" life insurance are excluded from the scope of MiFID II but a last-minute amendment to the level 1 MiFID II text amends the IMD on this point (hence IMD 1.5). Whereas MiFID II imposes a ban on third-party commissions for independent advice on financial instruments, as well as other provisions, the Commission will adopt level 2 measures on the distribution of insurance-based investment products and corresponding remuneration.

In preparation, the Commission requested technical advice from EIOPA on conflicts of interest in the distribution of insurance-based investment products. EIOPA delivered its advice to the Commission in February.

EIOPA has also consulted on conflicts of interest in direct and intermediated sales of insurance-based investment products, which included consideration of criteria for identifying types of conflict of interest that might harm customers; and steps to be taken in identifying, preventing, managing and disclosing conflicts of interest.

The Commission has asked EIOPA to refer closely to existing legislation (*i.e.* the MiFID implementing Directive 2006/73/EC) and to ensure cross-sectoral consistency by cooperating with ESMA, which is undertaking a similar exercise for all other investment firms.

Disclosures for non-life products

The IMD 2 proposals revise disclosure requirements for sales of non-life products. The Commission has proposed that, after a five-year transition period, intermediaries should disclose whether the payments they receive are on the basis of: (i) a policyholder fee; or (ii) a commission included in the insurance premium; or (iii) a combination of both. Intermediaries would also have to disclose the total remuneration, or at least the basis for calculation of the fee or commission.

The Parliament has resisted this approach, stating that intermediaries should only be required to disclose the source of remuneration, leaving the consumer to ask for more detailed information on request. EIOPA guidelines would be developed and Member States could maintain (or introduce) additional requirements, provided that distribution channels are treated equally, and the requirements are proportionate to the consumer benefits.

For direct sales, an insurance company would have to tell the consumer whether variable remuneration is paid to the employee for distributing and managing the insurance.

For large risks, both Commission and Parliament agree that no EU-wide disclosure requirements should apply. The definition of large risk remains as previously defined[25].

"Professional customers", as introduced by the proposal, would also not qualify for automatic EU-wide disclosure. However, the Parliament would significantly narrow categories of organisations on the list and would allow professional customers to request information from the intermediary regarding the "nature of the risk".

Adoption process

The three EU institutions (Commission, Parliament and Council) must agree before IMD 2 is adopted but Council has taken a long time to reach a negotiating position. The Parliament has been ready to negotiate since February 2014, notwithstanding the hiatus brought about by the European elections in May. Rapporteur Werner Langen was re-elected and reappointed without difficulty.

Successive Council Presidencies (Greek and Italian) have produced progressively more stringent positions than the Commission and Parliamentary texts. It is now for the Latvian Presidency to build a consensus. They are confident that this will be possible by May. Major points of potential conflict include "tying and bundling", treatment of commissions for independent advisors and home/host state supervision.

Key Information Document for Life Insurance Savings Products

New product disclosure requirements are complementary to the IMD 2 reforms, namely a Key Information Document (KID), which from 1 January 2017 consumers will receive before they buy a retail investment product, such as unit-linked life insurance.

The Regulation on key information documents for packaged retail and insurance-based investment products (PRIIPs) sets out the form and contents of the KID as well as the responsibilities of product manufacturers and intermediaries, and the sanctions and redress regimes.

Negotiations were challenging and there remain concerns over scope, disclosure requirements, the potential for arbitrage and, above all, the (over) elaborate contents of the KID. Many fear product manufacturers will not be able to meet their legal obligations and retain consumer interest in the document. If the document is too complex or incomprehensible, the entire exercise risks failing in its objectives.

To this end, the European Commission is undertaking consumer testing (Autumn 2014-August 2015). Customer understanding, preferences and engagement is being tested with volunteers from 10 Member States, including the UK, through on-line testing and focus groups. The first phase covers the presentation of: risk or reward; other risks; performance scenarios; and the cost calculation. A second phase of testing will take place after August with two model KIDs.

In the meantime, the ESAs are working with an expert group to develop draft:

- Regulatory technical standards (RTS) on The presentation of risk/reward and cost calculation (which will be adopted by the Commission as a Commission regulation or decision); and
- Technical advice to the Commission to assist it in preparing a delegated act on the presentation and content of the KID.

Consultation is expected in the third quarter so that delivery of initial RTS to the Commission is made by the end of the year and a second phase by March 2016.

Capital Markets Union

Part of the EU's economic recovery plan is a 315 billion euro investment fund. Another aspect is Capital Markets Union (CMU), which is currently open for consultation until May. An underlying objective is to increase and diversify the sources of funding available to the "real" economy thereby reducing reliance on bank financing. It covers a series of short, medium and longer term initiatives, including initial plans to revitalise securitisation and amend the prospectus directive.

The (re)insurance industry should reflect on the medium and long term aspects. For example, stakeholders are asked to give their views on measures to create incentives for institutional investors to broaden the range of assets they invest into. The Commission also seeks feedback on whether future reviews of Solvency II should target

[25] Article 13 (27), Solvency II Directive.

specific sub-classes of assets as part of the work on the tailored treatment of infrastructure investments, and whether introducing a standardised product could strengthen the single market in personal pension provision.

(Re)insurers may also wish to comment on cross-sectoral questions, such as the obstacles to integrated capital markets arising from company law and corporate governance requirements, insolvency laws or taxation. The review of the ESA powers will also, undoubtedly, catch (re)insurers' attention.

An action plan will follow this summer together with a timeline for putting CMU in place – currently programmed to run to 2019.

TAXATION

Global tax standards are changing, due to political pressure exerted by the G20 and G8 Leaders, based on technical work in the OECD. During the UK's G8 chairmanship in 2013, leaders made two commitments on tax fairness at the Lough Erne Summit which somewhat reinvigorated the international and European discourse, namely (i) "*to ensure that international and our own tax rules do not allow or encourage any multinational enterprises to reduce overall taxes paid by artificially shifting profits to low-tax jurisdictions*", inspired by the OECD-managed base erosion and profit shifting project (BEPS); and (ii) "*to developing a single truly global model for multilateral and bilateral automatic tax information exchange*", inspired by an OECD report advocating automatic exchange as the global standard for cooperation between tax administrations. The G20 launched the tax fairness initiative at their summit in Los Cabos in 2012 and confirmed it in St Petersburg in 2013. US pressure – via the Foreign Account Tax Compliance Act (FATCA) - also revitalised the global push. Both BEPS and automatic exchange are now key aspects of the international tax system.

Life Insurance in the EU

A major priority for the Commission has been to ensure that automatic exchange of information between tax authorities becomes the European standard for all forms of income. Recent European Council and ECOFIN conclusions attest to this commitment. Following a G-20 request, a global standard for automatic exchange was adopted last year, drafted by the OECD. Around 50 jurisdictions plan to exchange information using the new "Common Reporting Standards" by September 2017; and many more will follow in 2018. The EU legal framework applicable to savings-type life insurance is as follows:

- An amended Savings Taxation Directive (EUSD) adopted in March 2014;
- An amended Directive on administrative cooperation ("DAC"), adopted in December 2014; and
- Council decisions to revise Agreements which apply Union legislation on the taxation of savings and administrative cooperation in the field of taxation to certain jurisdictions and territories linked to EU Member States (the Savings Tax Network) - pending

Savings Taxation Directive (EUSD)

Proposals to revise the 2003 EUSD were published in 2008. They included provisions to expand the definition of interest income to include, for example, benefits from life insurance contracts. Tax authorities, using a "look-through" approach, would be required to take steps to identify who is benefiting from interest payments. By 2009, political agreement had been reached on most of the text, including the provisions on benefits from life insurance contracts.

Thereafter, negotiations focused on the third-country dimension, particularly arrangements with Switzerland. Here the negotiation remained at an impasse until March 2014, when the Directive was finally adopted.

Member States have until 1 January 2016 to adopt the national legislation necessary to comply with the revised EUSD. Benefits from a life insurance contract will be considered an interest payment for the purposes of the directive if the relevant life insurance contract was first taken out on or after 1 July 2014.

Directive on Administrative Cooperation (DAC)

The DAC was published in the Official Journal in April 2012 and Member States were bound to implement its provisions by 1 January 2013. It introduces automatic exchange of information from 1 January 2015 in five categories of income and capital, based on available information: income from employment, director's fees, life insurance products not covered by other EU legislation (*i.e.* the EUSD), pensions, and ownership of and income from immovable property.

During the negotiation process, Austria and Luxembourg – two Member States with rules on banking secrecy – secured exemptions. Luxembourg, for example, will not be exchanging information on life insurance.

A new DAC proposal was published in June 2013. It is concise and highly political in tone. The proposal extends the scope of the existing DAC to dividends, capital gains and any other financial income, and account balances. It removes the condition of "availability" for the new items as it is presumed this information is already exchanged with the USA under FATCA. The new DAC applies from 1 January, 2015 on taxable periods from 1 January, 2014.

Pressure to adopt the DAC proposal rapidly – in other words, before FATCA triggered a series of "most favoured nation" claims between the Member States based on Article 19 of the existing DAC – forced the Member States to agree to a staggered implementation date. As it concerned information not previously collected by Austria, it was agreed, Austria would have an additional year to prepare its IT systems. As a consequence, Austria will apply the provisions of the Directive from 1 January 2017 with respect to taxable periods as from that date.

Tax Fairness Agenda

The main question for the EU, in response to the OECD-managed BEPS project, is how to revitalize long-standing negotiations on the Common Consolidated Corporate Tax Base (CCCTB) proposal.

The existing framework is, however, seen as an insufficient response to BEPs. The LuxLeaks and SwissLeaks revelations in the press have also served to keep tax fairness in the spotlight. As a result:

- The Directorate-General for Competition has initiated investigations under EU competition (State aid) rules into a series of tax rulings in various Member States. Results will be known mid-2015 at the earliest; and
- A cross-Directorate working party led by the Directorate-General for Taxation has published its proposal for a new tax rulings directive.

Tax fairness is regularly debated in the Parliament. Following LuxLeaks, the ECON Committee is drafting two reports and has constituted a Special Committee on Tax Rulings and Other Measures Similar in Nature or Effect (TAXE). Results may be ready by autumn 2015.

Financial Transaction Tax

The Commission published proposals for an EU-wide Financial Transaction Tax (FTT) in September 2011. At the time, there was also considerable political pressure to impose such a tax globally. The Commission insisted on what it called the "triple A" approach. The tax would apply to:

- All markets (regulated markets or over-the-counter transactions);
- All instruments (shares, bonds, derivatives, etc.); and
- All actors (banks, shadow banks, asset managers, insurers, etc.).

By the end of 2012, it was clear that, for a variety of reasons, there would be no agreement between Member States, but that a group of eleven (EU11) would wish to pursue negotiations.

A revised proposal was tabled in February 2013. The scope and objectives are essentially unchanged except to account for the reduced geographical scope, but the anti-relocation and anti-abuse rules have been revised. There has been a great deal of criticism, including from the Council's Legal Service, and the EU11 appear far from agreement. Of the 17 Member States outside the negotiation, the UK is the most outspoken, having initiated court proceedings, which were subsequently dismissed by the CJEU as being premature.

It is not clear what the future holds for the FTT proposal.

Value Added Tax Review (VAT)

The VAT regime is being completely revised by the Commission. Based on plans set out in 2011, the Commission is working through a series of action points to review the system, make it simpler, more efficient and neutral, robust and fraud-proof.

In a recent report on tax trends the Commission highlighted the urgent need to make the VAT system more efficient. Member States have been steadily increasing their standard rate instead of either broadening the tax base or relying less on reduced rates. Further measures are necessary before the regime is fully effective.

JUSTICE AND FUNDAMENTAL RIGHTS

Background

The 2009 Lisbon Treaty transformed EU decision-making and enshrines the European Charter of Fundamental Rights in EU law. The Commission's Directorate General for Justice is responsible for a wide range of subjects such as civil and commercial law, consumer protection legislation, data protection and equality legislation, all of which can affect the (re)insurance sector.

Insurance Contract Law

There is no harmonisation of the law of insurance contracts in the EU[26]. This area of law remains a matter of national competence, but the Commission has been considering how to introduce a form of European contract law, while retaining national law, for more than a decade. The Commission is also reviewing differences in national contract law and whether these restrict cross-border trade in insurance products, and, if so, how any barriers may be addressed; an Expert Group on Insurance Contract Law, managed by DG Justice reported its findings[27] in January 2014.

In 2011 the Commission published a Communication (a non-binding policy paper), setting out the state of play and a proposal for a Regulation on an optional common European sales law ("CESL"). It is in the process of being adopted by the Commission, Parliament and Council, but is rather controversial and it is not certain when the process will be concluded. It does not cover insurance in its scope (since it governs cross-border contracts for the sale of goods, for the supply of non-financial digital content and for the provision of related non-financial services), but has provided additional impetus for closer consideration of obstacles to cross-border trade in insurance products.

Privacy and Cybersecurity

In 2012, the Commission published radical proposals to overhaul EU legislation and policy on protection of personal data. The proposals consist of a fully-revised Directive and a new Regulation. Their negotiation is highly sensitive, in particular following the emergence of certain practices in the social media sector, media revelations about the US government's monitoring of non-US citizens' communications, and high-profile data breaches, including in the (US) insurance sector. The revelations risk further complicating insurers' efforts to find solutions which enable them to process and transfer personal data according to client needs.

Once adopted, the EU personal data protection regime will force companies, including insurers and reinsurers, to revise the way they manage personal data. Fundamentally, companies must prevent hacking and other data breaches, or face significant fines. They must also analyse how they control and process personal data, particularly if they transfer such data to a third party located outside the EU.

Certain concepts in the proposals will set best practice in global personal data protection law; others are more controversial, or still require clarification. The proposals place new obligations on companies and the IT and other suppliers they contract with. This could pose difficulties, as personal information, including sensitive information, must be shared between many operators for the smooth servicing of an insurance policy. As the proposal is currently drafted, legal liability may be difficult to determine for each party.

Of additional concern is the treatment of international transfers, *i.e.* out of the EU to "third countries" (such as the US). Certain data such as health data, vital to travel and health insurance, are considered "sensitive data" and may be particularly vulnerable to stricter rules, particularly following comments by senior EU politicians suggesting that localisation of data within the EU is the logical response to the NSA/PRISM incident.

A wide range of market operators comes within the scope of a proposal for a Directive for network and information security across the Union, the NIS Directive, whose purpose is to improve the security of the internet, private networks and information systems. Insurers, reinsurers and buyers of cyber insurance, will need to take "state of the art" technical and organisational measures to manage their security risks and be ready to report significant security breach incidents. Once in force, the legislation will complement existing legislation affecting telecommunications network and service providers, and critical infrastructures, as well as the legislation adopted under the EU Cyber Security Strategy, such as the directive on attacks against information systems which outlaws the use of botnets, malicious software and illegally-obtained passwords.

DISPUTE RESOLUTION

Alternative Dispute Resolution

Legislation on Alternative Dispute Resolution (ADR in the form of a directive) and Online Dispute Resolution (ODR – a regulation) was published in June 2013.

The Commission had put forward legislative proposals following years of cajoling to encourage the development of schemes across the EU. Few Member States have no ADR at all, but few have schemes for all sectors. Most have a mix of public and private schemes, of varying quality. The public is not generally aware of what exists and business

[26] Though note EU legislation on jurisdiction and enforcement of judgments (the Brussels I bis Regulation) and on the law applicable to contracts, including contracts of insurance (the Rome I Regulation), as well as the harmonised rules on certain pre-contractual disclosures (*e.g.* Articles 183-186, Solvency II Directive).
[27] http://ec.europa.eu/justice/contract/files/expert_groups/insurance/final_report_en.pdf

tends to be reluctant to participate, despite the potential cost-savings.

Consumers seeking redress from financial institutions may find further information about national schemes from the EU Financial Dispute Resolution Network (FIN-NET). Current members come from only 22 of the 28 EU Member States, as well as the three EEA/EFTA countries, with some countries hosting more than one scheme. However, as Member States must implement the new legislation by July 2015, new schemes should be introduced imminently where they are currently lacking.

An EU-wide platform to resolve cross-border disputes will be set up, based on the ODR Regulation. Although cross-border disputes are currently at a relatively low level, they may rise as more commerce is conducted on-line. The ODR platform should be operational by January 2016. Meantime, FIN-NET continues to process cross-border complaints using an on-line form, available from its website.

Community collective redress (CCR) – EU jargon for class actions – is a much more sensitive topic. Although supported by consumer groups, the Commission has avoided binding proposals. In June 2013 it published a Recommendation (a set of common, non-binding principles) for the Member States, which are encouraged to set up national mechanisms, including for financial services. The Recommendation complements the Directive on antitrust damage actions, designed to encourage private enforcement, which applies from December 2016.

Finally, as noted above, EIOPA has an increasingly important role in the EU institutional structure. Its activities are dominated by Solvency II implementation. A consumer protection focus is also evident in its work on the distribution of insurance-based investment products.

With reference to the section on "New Instruments", the ESAs have constituted a Board of Appeal to give parties right of redress against ESA decisions. The decisions of the Board of Appeal can be appealed to the CJEU. It is early days, there have been just four decisions. However, as Solvency II, and other financial services legislation develops, recourse to this Board may increase.

Litigation

As described above, the EU institutions are in the process of revising requirements for pre-contractual disclosures. In previous years, the Commission used "*market evidence of a very high number of complaints*" in France and Hungary, and an example of mis-selling of equity-linked insurance products in the Netherlands as justification for its IMD 2 and PRIIPs proposals. Similarly, it is a well-known phenomenon that, as soon as the Commission begins to develop policy in a given area, national legislatures and competent authorities frequently intervene with their own initiatives in order to "stake their claim" and shape the debate. By way of example, certain Member States have already extended MiFID-type rules to the life insurance sector.

At the same time, national and EU supervisors have been active in alerting consumers to the risks inherent in financial products, including certain insurance contracts[28].

The insurance and reinsurance sector is not a serial litigator before the CJEU. Cases are sporadic. There have been few in 2014:

- The *Baradics*[29] request for a preliminary ruling concerns package travel and insurance in case of insolvency of the travel operator. The appellants claimed Directive 90/314/EEC on the subject had not been properly transposed into national law. The Court recalled that it was for national courts to determine whether national provisions were adequate; and
- The *Generali-Providencia Biztosító Zrt*[30] case which concerned grounds for exclusion from a public procurement tendering procedure to provide insurance services. The appellant was excluded from the procedure due to a previous national competition law infringement which had been confirmed by a court judgment. The court held that the EU Treaties do not prevent a national authority from applying such an exclusion.

POLITICAL OUTLOOK

Given the range and potential effects of the various proposals summarised above, it is evident that 2014 was an intensive period for EU law-making and supervision. Many (re)insurers have faced the dual challenge of keeping abreast of developments under current law while watching the horizon, and reacting in a timely fashion to proposals with direct and indirect effects on their business.

[28] In 2013 EIOPA issued two opinions on payment protection insurance and beneficiary protection arrangements regarding life insurance contracts. In 2015, an opinion was published on sales via the Internet? Further details at: https://eiopa.europa.eu/publications/eiopa-opinions

[29] Case C-430/13, Ilona Baradics and Others v QBE Insurance (Europe) Ltd.

[30] Case C-470/13, Generali-Providencia Biztosító Zrt v Közbeszerzési Hatóság Közbeszerzési Döntőbizottság.

2014 was a year of political change. The European elections took place in May and the new Commission and other senior appointments were completed in November.

On 1 January 2015, Latvia assumed the new Presidency of the Council of Ministers for the first time. Luxembourg will take over in July.

This is not, however, business as usual. No one appears satisfied with the status quo, all want change. This is reflected in the new Commission's work programme and working methods, which are generally more collaborative with Commissioners working in teams and across the Directorates-General to deliver (fewer) packages of legislation and policy papers. There appears to be closer cooperation between the Commission, Parliament and Member States, and greater emphasis on transparency and ethics. However, this is all underpinned by prolonged economic uncertainty most evident in Greece, conflict at the border, and serious doubts in some quarters that the EU is where they want to be.

CONCLUSION

The previous Commission, Members of the European Parliament and Council have left behind more than 40 separate financial services texts, some of which are still being negotiated or require EU-level implementing measures. Progress on a selection of those of most interest to the (re)insurance sector has been outlined above. This body of work, together with control of state aid to individual financial institutions in difficulty, represents the EU response to the global financial crisis.

At the start of the new term for the Commission there is a distinct shift in attitude, away from fire-fighting the crisis towards recovery. Commissioner Hill, who is responsible for financial services, including insurance and reinsurance, has already indicated a willingness to review and examine the cumulative effect of rules adopted since the financial crisis.

CONTACT

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This information should not be treated as substitute for specific legal advice on individual situations.

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