The greatest opportunity perhaps, however, lies in **"REHABILITATION"** - a challenge which no liability insurer can surely ignore and which every shareholder in every insurance company must whole-heartedly welcome. It can properly be argued that it is the only realistic technique presently available for the abridging of the ever escalating claims in cases of injury of maximum severity. It is a topic which should surely be on the agenda of every board meeting of every insurer. It goes hand-in-hand with "structured settlements".

Thus those theories of yesteryear as to the role of the law of tort - theories born of an era which believed in the bottomless pocket - such theories are as outdated as communism and the Berlin Wall.

We as tort lawyers can raise our heads and say with confidence: "These Truths We Hold To Be Self-Evident - the 1960s are dead: OK?"

2. EC
by Patrick Devine, Clyde & Co.

As our chairman has indicated it is my task this morning to offer an update on legal developments in EC insurance law in the past twelve months.

This would be a daunting prospect at the best of times - and not just because I am aware that I am addressing such a distinguished company.

My main difficulty with this presentation is that this is, of course, 1992 and the Community's institutions have been particularly busy in bringing forward the legislation identified as necessary to create the Single Insurance Market from January 1st 1993.

Before I go any further I want to say a word about the proposed Maastricht Treaty which has been the focus of much debate in the media recently. What does Maastricht mean, if anything, for insurance if it proceeds to ratification in the Member States?

There are no direct implications for insurance. The agreement is mainly concerned with:

- foreign policy;
- economic and monetary union;
- subtle changes to the balance of power of the Community institutions.

It is the latter which is of indirect importance to the insurance industry because the European Parliament will, as a result of the Maastricht Treaty, have the right to reject Community legislation.

This means that the insurance industry will have to lobby the Parliament more effectively than it has in the past. The European Parliament has traditionally been the most consumer oriented of all the Community institutions. It has been at liberty to adopt that role as in the EC legislative process it has traditionally had neither power nor responsibility.

It will be interesting to see whether, as a result of the Maastricht Treaty, it becomes more influential and less consumer orientated.

I shall now return to my task. The Community has adopted all but two of the insurance Directives listed in the Commission's 1985 Single Market legislative programme.

It has failed to advance the controversial:

- Proposal for a directive on insurance contracts, ((COM (79) 355 modified by (COM (80) 854)), and

- Proposal for a directive on the winding - up of insurance companies.

The Commission has, however, in other respects far exceeded its brief.

Given the time available to me and the volume of notable developments which have taken place this year I can, as I am sure you will appreciate, give no more than a tour d'horizon of the key events of 1992.

I propose to offer (1) a few brief comments about two key judgments of the European Court (2) a review of the main EC legislation introduced this year (3) a few words on the developments between EC and EFTA insofar as they impact upon insurance, and (4) finally, if there is time, a look to the future.

1. THE FRANCOVICH JUDGMENT

(*Francovich and Boniface -v- Italian Republic*, Judgment 19 November 1991 Joined cases C-60/90 and C-9/90. The Times 20 November 1991).

I shall say a few words about the European Court's judgment in *Bachmann* in my con-

cluding remarks and at this juncture shall confine my comments to the Court's judgement in *Francovich.*

The failure by Member States to implement EC legislation in their national law - either properly or at all - has long been regarded as a problem which the Community is now taking active steps to resolve.

The Commission now has an action plan for the exchange of national officials engaged in the enforcement of Community legislation and the Maastricht Treaty will (if ratified) allow the European Court to fine Member States who fail to implement EC legislation.

In its landmark judgment in *Francovich* the European Court has assisted the processes of implementation and enforcement by creating a new right of action allowing private parties to claim compensation from Member States which fail to implement EC Directives. *Francovich* was not an insurance case but the judgment has implications for the creation of the single market.

As a result of Italy's failure to implement a 1980 Directive protecting employees in the event of the insolvency of their employer (Directive 80/987) Francovich and other employees, in effect, were treated not as preferred creditors following the insolvency of their employer but as general creditors.

The employees were therefore unable under Italian Law to recover from the liquidator the pay and other compensation they were entitled to by their contracts of employment. By finding that a State is liable in damages to a private individual, the European Court effectively overruled the Court of Appeal's judgment in *Bourgoin -v- Secretary of State* (1986) Q.B. 716.

As a result of the judgment, for an individual - and that includes companies - to recover damages from a Member State arising from the non-implementation of a Directive, the individual or company must show that:

- the Directive sought to confer rights upon individuals (not all do so), and
- those rights are ascertainable from the provisions of the Directive itself, and
- there is a causal link between the failure by the Member State to fulfil its duty to implement the Directive and the loss suffered by the individual.

That much is reasonably clear. Other aspects of the judgment and its consequences are less clear.

The judgment has a number of possible implications.

1.1 Extension to the incorrect implementation of Directives?

The judgment was handed down in the context of a case concerning the *failure* to implement a Directive. The European Court's reasoning suggests that the right of action could be extended to include a right of damages where a Directive was *incorrectly implemented* in national law.

1.2 Extension to a right of damages against a Member State for any other breach of Community law?

The Court's decision also referred to the co-operation incumbent upon Member States to fulfil the requirements of Article 5 of the EC Treaty.

Article 5 requires Member States to take all appropriate measures to ensure that they fulfil their obligations under the Treaty and to abstain from any measure which could jeopardise the attainment of the Treaty's objectives. This suggests that the right to claim damages against a Member State could be extended to include breaches of EC law other than Directives i.e. any breach of EC law.

The judgment opens up a number of possibilities for the insurance industry. It will be interesting to see how this right of action develops through further decisions of the European Court and domestic courts.

One of the problems is identifying the Defendant. The action lies against "the State", a term which in Community law includes local government, central government and other arms of the State, and not just "the crown" as under English law.

2. LEGISLATION

In terms of legislation, the Community has moved forward this year on a very broad front. We have witnessed the advancement of a number of key Directives, the first Recommendation to be introduced in the insurance sector and an important draft Regulation.

2.1 The Insurance Accounts Directive

(Directive 91/674/EEC 19 December 1991).

The DTI circulated a Consultative Document on the Insurance Accounts Directive on June 23 of this year, setting out the government's position and seeking views.

It will be recalled that this Directive applies to all insurance and reinsurance companies, Lloyd's, mutuals and certain Friendly Societies (i.e. those covered by the 1987 Regulations) and applies to both life and general insurance undertakings requiring that all accounts give a "true and fair view" and demanding disclosure of hidden reserves.

2.2 The Motor Services Directive

(OJ No. L330/44 29 November 1990).

Council Directive 90/618/EEC of 8 November 1990,amending Directives 73/239 and 88/357, particularly as regards Motor Vehicle Liability Insurance.

Adopted on 8 November 1990 this Directive is due to enter into force by November 20 of this year. The Motor Services Directive brings motor insurance in to the existing arrangements for freedom of services for non-life insurance and allows motor insurers to write business on a "large risks" services basis if they join the local Motor Insurers' Bureau and guarantee fund.

"Mass risk" motor cover can be provided on a services basis but may still be subject to an administrative authorisation in the State where the risk is situated (i.e. where the vehicle is registered).

Insurers must appoint a local representative to deal with claims.

The Directive also contains rather weak "reciprocity" provisions designed to open up non-EC insurance markets to EC insurers. These provisions are not confined to motor insurance but are of more general application.

2.3 The Third Generation of Insurance Directives

These take the form of:

- **The proposed Third Life Assurance Directive**
  (OJ No. C196 3 August 1992)

A Common Position was reached by EC Council Finance Ministers on June 29. Adoption by end of year is expected.

- **The Third Non-Life Insurance Directive**

(Council Directive 92/49/EEC of 18 June 1992 OJ No. L228/1. 11 August 1991.)

Adopted on 18 June. Due to enter into force by 1 July 1994.

Each of these so-called third generation Directives substantially amends their two respective predecessors in order to create a regime characterised by "Home State control", a single licence or authorisation under which branches and agencies are supervised by the Home State regulatory authority and the prohibition of prior approval of policy terms and premium rates.

The implementation of this legislation in English law will require considerable amendment to the Insurance Companies Act 1982 and regulations issued thereunder and we must by now be reaching the stage where a new consolidated Act is inevitable.

Limitations of time demand that I must be selective and I wish to offer a few comments not upon the Directives I have just referred to but to other significant EC legislation introduced this year.

2.4 The Commission Recommendation on Insurance Intermediaries

(OJ No. L19/32 28 January 1992)

The calendar year began with the publication of the European Commission's Recommendation on Insurance Intermediaries. The Recommendation is worthy of note on a number of grounds, not least that it is the first Recommendation to be issued in the insurance sector.

A Recommendation is not legally binding. Member States are therefore merely "encouraged to introduce the provisions of this Recommendation into their national law by January 1995. The Member States will, however, be aware that if they fail to do so the Commission may introduce a binding Directive in due course.

National courts are obliged to take the provisions of the Recommendation into account where relevant.

The Single Market legislative programme did not provide for any legislation for insurance intermediaries. The Recommendation was introduced because, notwithstanding the Brokers and Agents Directive of 1977 (Directive 77/92), some Member States (Denmark and Germany) still have no legislation regulating the conduct of business by insurance intermediaries.

While the majority of Member States do maintain laws regulating the conduct of business by insurance intermediaries they are neither consistent nor co-ordinated and do not provide for common standards of consumer (policyholder) protection throughout the Community. This inconsistency was perceived by the Commission as a threat to the distribution of insurance through these channels in the single market.

Also notable is the fact that the Recommendation applies to **all** persons mediating in insurance i.e. independent brokers, part-time agents and tied agents, as well as bank or building society counter staff. In future all such insurance intermediaries throughout the Community will have to be registered either with their employer or relevant professional body. Any person or company not registered will not be allowed to engage in business as an insurance intermediary.

In addition, all insurance intermediaries must satisfy minimum standards of education and experience at a level determined by the individual States and they must be able to establish that they are of "good repute" i.e. not previously declared bankrupt unless the bankruptcy has been discharged.

They must also hold professional indemnity insurance (or an equivalent guarantee) against liability for negligence.

In the interests of policyholder protection one of the main objectives of the Recommendation is to ensure that there is a clear distinction between independent and dependent (or "tied") intermediaries who distribute the products of one or a limited range of life or non-life undertakings. This is provided for by imposing a duty upon independent brokers to declare to policyholders any direct legal or economic ties they have with insurers which might affect their choice of policy. How and to what extent and with what frequency these ties must be disclosed is not specified in the Recommendation. It is left to the individual Member States to determine.

Independent brokers must also disclose their spread of business to the relevant competent authority each year.

The effect of the Recommendation will be most strongly felt in e.g. Germany and

Denmark which, as stated earlier, do not currently have legislation regulating insurance intermediaries.

All Member States will, however, have to change their laws if they are to implement the Recommendation. For example, in the UK only "brokers" must be registered (with the IBRC) at the present time. Once the Recommendation is implemented all insurance intermediaries will have to be registered.

A DTI Consultative Document on the Recommendation is expected later this autumn.

2.5 Public Procurement : Insurance

Council Directive 92/50/EEC of 18 June 1992 relating to the co-ordination of procedures for the award of public service contracts (OJ. L 209/1 24 July 1992).

July saw the publication of Council Directive 92/50/EEC relating to the co-ordination of procedures on the award of public service contracts. Insurance is one of the financial services falling within the scope of this Directive which is due to enter in to force by July 1 next year. A DTI Consultative Document will be circulated in the autumn.

The purpose of the legislation is to open up the EC market for the placing of public sector risks and to encourage cross border competition between insurers serving this sector.

It provides for a regime under which central, regional and local government - as well as state and semi-state entities - purchase insurance cover. It is the first EC legislation to dictate how insurance must be bought and a broad range of entities will be affected by the Directive e.g. education and fire authorities, the police, NHS, certain development and enterprise agencies and the Post Office.

The Directive will apply to local authorities in particular as they often award 5 year contracts and it is the aggregate premium over that term which used to calculate the **400,000** ECU premium threshold which determines whether the Directive applies or not. It is thought that more than 80% of the UK's 500 plus local authorities will be subject to the Directive.

There is no question that both insurers and brokers serving this sector will have to become familiar with the terms of the Directive and to review the way they have traditionally done business with this sector.

Failure to comply with either the procedure or the timetable laid down in the Directive may result in damages being awarded against the insured whose duty it is to comply with the Directive's requirements.

The remedies available for breach do not allow for policies to be declared void or unenforceable because of a failure to follow the procedures of the Directive. But it should be noted that in two cases before the European Court the Court has overturned contracts awarded in breach of the parallel Public Works Directive.

Procedures

The Directive applies to direct insurance policies where the premium payable exceeds 400,000 ECU. It does not apply to either reinsurance or captives.

Basically, there are three procedures which must be followed by a public authority when purchasing insurance.

These are the Open procedure, where all interested insurers may submit a "tender" or quote, the Restricted procedure, where only insurers invited by the potential insured may quote, and the Negotiated procedure. The Negotiated procedure allows the potential insured to consult with a minimum of three insurers and to negotiate the terms of the policy with one or more of them.

Procedural Time Limits

These procedures must be followed within strictly defined time limits. For example, under the Open procedure the offer for invitations to tender to provide the insurance cover or other insurance services that might be required, must be kept open for between 36-52 days.

Under the Restricted and Negotiated Procedures one is dealing with fewer insurers and the equivalent period is 26 or 37 days.

The shortest period is reserved for "urgent cases" where insurance cover is needed quickly. The time limit means that emergency insurance cover cannot be secured in less than 10 days.

It is the negotiated procedure which accords most closely with current market practice where a policy is secured through the services of a broker or in direct negotiations with a number of insurers. Unfortunately, however, the negotiated

procedure can only be relied upon under limited circumstances for example:

- "in exceptional cases, when the nature of the services of the risks involved do not permit overall pricing" (Article 11.2(b)).

Many of the provisions of the Directives are as vaguely worded as this one.

This Directive will prove problematic in practice not least because the regime of the Directive is not specifically structured to the demands of insurance or the practices of the market. It follows the pattern of the Public Works and Utilities Directives, which are themselves based on GATT documentation.

The new insurance purchasing regime will be expensive to administer, given the obligation to maintain records of how decisions are reached and the obligation to publish invitations to tender in the Community's Official Journal.

There is, moreover, considerable potential for spoiling tactics and litigation not only because the meaning of some of the most basic provisions of the Directive remain open to interpretation, but also because insurers who are not successful in securing the award of the contract are entitled to a written explanation stating the name of the successful tenderer and the reasons for the rejection of their tender. Unsuccessful insurers are usually not advised as to why they were rejected in favour of another insurer. The Directive gives them a legal right to know.

Care should therefore be taken when giving such reasons as a letter carelessly drafted might reveal that the full procedure or time limits were not complied with and could result in the entire procedure being re-opened.

The EC's proposed public procurement regimes have been the subject of much criticism and it is more than likely that both current and proposed legislation in this area will be amended.

2.6 Competition and Insurance

(OJ No. 92/C207/2 14.8.1992 Communication pursuant to Article 5 Council Regulation (EEC) No. 1534/91 of 31 May 1991 on the application of Article 85(3) of the Treaty to categories of agreements and concerted practices in the insurance sector).

The most recently published initiative from the Commission can be found in the Official Journal of 14 August. It is the draft Regulation outlining the types of

agreement and collaboration in the insurance sector which will be exempted from the Article 85 (1) of the Treaty, the Community's main anti-cartel provision.

The draft expressly disapplies Article 85 (1) to collaboration by insurance and reinsurance companies with respect to:

- the establishment of common risk premium tariff based on statistics which they collate together or their claims experience;

- the establishment of common standard policy conditions;
- the common coverage of certain types of risks;
- common rules for the testing and acceptance of security devices.

It should be noted, however, that these exemptions are only available if the conditions which form the main body of the draft are fulfilled.

So, for example, collaboration between co-insurance and co-reinsurance groups will only be exempt by the Regulation if the participant co-insurers together have a share of less than 15% of the relevant market and cover catastrophe risks. The market share percentage is reduced to 10% for other co-insurance groups.

Likewise standard policy conditions and standard models illustrating the future benefits of a life policy will only be exempt if they are not binding on the participants but serve purely as models. The Commission seeks comments on the draft by September 23rd.

2.7 Environmental

Finally, I would like to mention one important Directive which does not appear to be proceeding at all. This is the Proposal for a Directive on Civil Liability for Damage Caused by Waste.

This proposal you will recall is based on the principle the "polluter pays" and seeks to impose an EC-wide regime of liability for "producers" of waste which causes personal injury, death, property damage or "impairment of the environment".

The environment is damaged where it suffers "significant physical, chemical or biological deterioration".

The prospect of joint and several liability, retrospective liability, liability for clean-up

costs, the imposition of a compulsory insurance requirement and the possibility (at the discretion of Member States) that interest groups such as Friends of the Earth or Greenpeace would be given locus standi, have ensured that the Proposal has received much attention.

The Proposal was subjected to heavy criticism from the insurance industry. My understanding is that - discretion being the better part of valour - the Commission is not advancing its proposal but would prefer to see it overtaken by a Convention being negotiated outside the framework of the EC at the Council of Europe.

The Council of Europe are currently negotiating a new Convention entitled the Draft Convention on Civil Liability for Damage Resulting from Activities Dangerous to the Environment. (Council of Europe, Strasbourg - 31 July 1992 DIR/JUR (92) 3).

Its aim is to provide:

- adequate compensation for damage resulting from activities dangerous to the environment, and
- to provide a means of prevention of damage and,
- reinstatement of the environment

It has a number of features in common with the EC's proposed Directive e.g. it provides for compulsory insurance or other financial security for "operators" conducting a dangerous activity but allows national law to dictate the limit of cover required.

It is clear that some attempt has been made to avoid the criticisms levelled at the Community's proposal. For example, the liability provisions of the draft Convention seek to exclude retrospective liability by providing that the liability provisions will only apply:

"to damage caused by occurrences or part of a continuous occurrence taking place after the entry into force of the Convention". (Article 5.1)

The wording of this exclusion may not prove to be adequate but it is at least an improvement upon the vague term EC's Civil Liability for Waste Proposal. In addition, it is intended that no liability will attach to permanent waste dumps which are:

- closed before the entry into force of the Convention, or

- where the operator can prove that the damage was caused solely by waste deposited there before the entry into force of the Convention.

The mere fact that such liability is excluded from the draft Convention does not of course exclude the possibility of liability attaching under domestic law.

This draft Convention does not represent a wholesale shift of authority from Brussels to the Council of Europe in Strasbourg but it is clear that the focus of attention for lobbyists will have to encompass both Brussels and Strasbourg.

3. EEC-EFTA-EEA

In the broader framework of things the single most significant event of the year must be the Draft Treaty on a European Economic Area between the 12 EC Member States and the 7 EFTA countries - **Norway, Sweden, Finland, Iceland, Switzerland, Austria** and **Liechtenstein.**

This will extend the single market and create one European Economic Area (EEA).

As far as I am aware the final text of the agreement has not yet been published and the all important annexes listing the EC legislation which the EFTA countries will adopt are still under discussion. It is, however, understood that the EFTA countries will adopt EC law to ensure the free movement of **goods, services** and **capital,** together with those rules regulating **competition,** the **environment, company** law and **consumer protection.**

The EC Treaty - given rights of establishment and freedom to provide services will be accorded to EFTA insurers who will be treated in future as EC insurers.

It is, also clear that by 1st January 1993 the EFTA states will implement **all** insurance Directives adopted by the EC **before 1 July 1991.**

This means that by January 1 1993 they must implement the greater part of EC insurance legislation in their national law.

This includes by way of example:

1. the 1964 Directive abolishing restrictions on the freedom of establishment in reinsurance and provision of services in reinsurance and retrocession - Directive 64/225.

2. The First Life and Non-Life Establishment Directives.
3. Tourist Assistance Directive 84/641/EEC.
4. Credit Insurance Directive - 87/343/EEC.
5. Legal Expenses Directive - 87/344/EEC.
6. The Second Non-Life Services Directive - 88/357/EEC.
7. The Motor Services Directive - 90/618/EEC (and earlier Motor Liability Directives)

No major amendments to the terms of these Directives are planned, although they will be slightly amended to accommodate individual EFTA States. For example, the **First Non-Life Directive 73/239** does not apply to local fire insurance monopolies in Germany and France. It will also not apply to the monopolies found in Switzerland and Ireland.

With the implementation within EFTA of the **Second Non-Life Services Directive 88/357** Non-Life insurers will be free from 1st January 1993 to provide "large risk" cover on a services basis to all EFTA countries. They need only comply with a simple notification procedure before doing so.

UK insurers will be able to save on administrative costs by closing down branches and agencies in EFTA countries covering risks located there on a services basis from London or elsewhere in the Community.

The threshold adopted by the EEA is the lower second stage threshold i.e. a large risk policyholder is defined as an undertaking satisfying two of the following three criteria:

- balance sheet total : 6.2 million ECU
- net turnover : 12.4 million ECU
- an average of 250 employees employed during the financial year

By adopting the thresholds they also inherit the defects in the thresholds. The need to show a balance sheet or net turnover generally means that the company insured must have been trading long enough to have filed accounts.

If the policyholder is a brand new company or subsidiary it will not necessarily have filed accounts and so will not have either a turnover or balance sheet total and may not therefore be able to satisfy the "large risk" criteria. This is a particular problem when seeking to insure new subsidiaries of companies with their Head Office outside the EEC which do not file consolidated accounts within the Community.

Directives not adopted by the EC before July 1 1991

When will the EFTA States implement the Directives adopted by the EC after July 1 1991? I understand that EFTA has exceptionally agreed in principle to implement both the **Insurance Accounts Directive** and the **Insurance Intermediaries Recommendation** by January 1 1993. It has also agreed to implement the **Third Non-Life** and **Proposed Third Life Directives** at the same time as we do in the UK (i.e. July 1 1994 for the Third Non-Life Directive).

Realistically, we can expect one or more EFTA States to seek to delay the implementation of these third generation Directives for a year or two.

4. THE FUTURE - POST 1992 DEVELOPMENTS

Finally, what developments can we expect in the near future - post 1992? The activities of the European Commission will, I believe, concentrate upon are:

4.1 The removal of remaining obstacles to the Single Market Taxation

The Court's judgment in **Bachmann** in January of this year has focused attention on the need to co-ordinate taxation within the Community more closely, particularly as it affects life policies.

The Court upheld a Belgian law which allowed premiums payable on life assurance policies to be tax - deductible only if they were paid to a Belgian insurance company.

This rule clearly discriminates against foreign life assurers but was upheld by the Court on the ground that it was a justified restriction on the application of Articles 48 and 59 of the Treaty in view of the overriding need to maintain the "cohesion" of the Belgian fiscal system.

The Commission's work in this area is also likely to involve a review of the Member States' premium tax regimes. Without doing violence to the right of States to impose premium taxes, there is also ample scope for closer co-ordination and simplification of Member States' premium tax regimes e.g. who must pay them, when and how and the problems of apportioning taxes between two or more states.

Winding-up

A draft insolvency convention was proposed by the Council of Europe last year. The

European Commission does not favour it and we might see new life being injected into the Commission's proposed Directive on the winding-up of insurers. Negotiations on this proposal have come to a halt since a Commission amendment was proposed in 1989. (Commission Proposals (COM(86) 768) and (COM(89) 394)).

4.2 Supervision of conglomerates

The second area which we can expect to receive attention is the supervision of financial services conglomerates.

"Bancassurance" and **"Allfinanz"** - the offering of insurance and other financial services by banks, insurers and investment houses - have highlighted the need for closer co-operation between bank regulators and insurance regulators.

How does one classify "Bancassurance" for example and who should supervise it - insurance regulators or bank regulators? With banks competing with insurers as distributors of many personal lines products it is possible that this debate will become quite heated and any change in favour of the banks is likely to meet strong resistance from the insurance industry.

3. LEGAL UPDATE ON REINSURANCE CASES

By John Thomas Q.C.

The past year has seen a number of cases dealing with reinsurance topics. I will deal briefly with some of the more important – nothing really new, just a discussion of some old chestnuts.

Use of a Slip in Construing a Treaty

One of the most interesting judgments in the past 12 months was the judgment of the Court of Appeal given in February in *Youell v. Bland Welch. The Super Hulls Case* [1992] 2 Lloyd's Rep. 127 The case concerned the reinsurance of the construction risks of LPG carriers under construction at the Avondale Shipyard and a claim in the 1970s made under that reinsurance by the insurers of the vessels. The detailed facts of the case are of no intrinsic interest and the other part of the case, namely the claim against the brokers for negligence was no doubt dealt with at last year's conference; the appeal against that judgment was compromised during the course of the hearing in the Court of Appeal.