



Key messages on the Insurance Block Exemption Regulation

Introduction

The Insurance Block Exemption Regulation (“IBER”) is a sector-specific legal instrument which allows (re)insurers to benefit from an exemption to the prohibition of anti-competitive arrangements laid down in Article 101(1) of the Treaty on the Functioning of the European Union (“TFEU”).

The exemption covers two types of agreements between (re)insurance undertakings:

1. Agreements with respect to joint compilations, tables and studies; and
2. Common coverage of certain types of risks (co/re insurance pools).

The IBER expires on 31 March 2017 and the Commission is considering whether it should be renewed, either in whole or in part. The Commission is required to submit a report on the functioning and the future of the IBER to the European Parliament and the Council by March 2016.

To this effect, the Commission has held a public consultation, inviting stakeholders to submit relevant information on the functioning of the IBER, and their views on whether the Commission should renew any of the IBER provisions in a new block exemption regulation. Following the consultation, the Commission sent targeted questionnaires to affected stakeholders. It is holding bilateral stakeholder meetings in 2015 and will undertake a public consultation on the option chosen in the second half of 2016. The Actuarial Association of Europe (“AAE”) submitted a response to the consultation in November 2014.

Purpose

The purpose of this short paper is to reiterate the key views of the AAE and to seek to influence the process as the time for decision draws near.

Opinion

The AAE is supportive of the retention of the elements of the IBER which it believes are important to the efficient functioning of insurance markets. The AAE represents the actuarial profession in Europe. As the profession which bears most responsibility for the pricing/underwriting of and reserving for insurance risks, the actuarial profession has considerable experience of the benefits which the IBER has provided for the industry and, by extension, the consumers of its products.

Agreements with respect to joint compilations, tables and studies

Requirement for statistical tables

Insurance is a fundamental need of society and allows individuals and companies to manage their risks in an economic way. The optimisation of economic benefit for consumers of insurance requires that the market for insurance be as efficient as possible. Efficiency is enhanced where insurers have a clear picture of the cost of the risks which they propose to cover. This facilitates informed pricing and reserving, enabling additional loadings to reflect risk of mispricing to be kept to a minimum. The availability of joint compilations, tables and studies relating to underwritten risks is a cornerstone of informed pricing and reserving. The IBER facilitates the execution of such studies. There is considerable evidence around Europe of studies relating to both life and non-life insurance.

Competition

The existence of the IBER does not act to reduce competition in insurance markets. That is evidenced by the strong level of competition which can be observed in European markets. Informed pricing is itself a facilitator of competition in that it puts the focus in pricing differentiation on the elements which are company-specific and therefore should be subject to competition.

These elements are:

- Differentiation in cost of risk from market due to difference in approach to underwriting or claims, e.g. different approaches to no claims bonus for motor insurance.
- Risk appetite, driving the risk loading added to anticipated risk cost.
- Expense loading.
- Profit margin.

The contention of the AAE is that joint compilations, tables and studies promote rather than inhibit competition.

Solvency II

The new Solvency II regulatory regime, which comes into full force on 1 January 2016, incorporates a requirement for (re)insurance firms to provide for an effective actuarial function¹, of which the primary responsibilities include:

- Coordination of the calculation of technical provisions; and
- Expressing an opinion on the overall underwriting policy.

Establishment of technical provisions in respect of (re)insurance business requires the calculation of a “best estimate liability” which is the value, incorporating a best estimate of assumptions as to the ultimate experience in respect of the main variables, of the liabilities undertaken.

Insurers are in possession of their own data covering experience on insurance business which they have written.

¹ Directive 2009/138/EC – Article 48

However, in many if not most cases this will not be adequate to establish best estimate assumptions, for the following reasons:

- Insurers' data relates to their own experience. In setting best estimate assumptions, actuaries value inputs from wider market to establish, for instance, whether there is any variation in the experience of the firm from the wider market which may mean that current experience is misleading.
- New or small insurers may have too little data (either in terms of their share of market or duration of experience) to be representative of likely future experience.

Other elements of Solvency II requirements which will benefit from the availability of representative statistical tables include the requirement for a regular Own Risk and Solvency Assessment, which is required to include a comprehensive study of the risks to which firms are exposed, including the application of stresses to all parameters, as well as a study of the appropriateness of the standard formula for the calculation of firms' solvency capital requirement.

New entrants

In assessing whether to enter new markets, firms will study the extent to which their enterprises can be profitable. Market rates ("what must I charge?") and market experience ("what will it cost?") are equally important elements of this equation. Without access to market statistics, it will not be possible to establish costs of covers to be provided with sufficient certainty to enable new entrants to price effectively. This barrier to new entrants has the potential to inhibit competition. Facilitation of new entrants and of competition in general encourages greater diversity of participants in insurance markets and provides greater capacity for insured risks.

Big Data

In the age of Big Data, ownership of data increasingly confers a competitive advantage. This is particularly the case with (re)insurance where data is the raw material for pricing. In the absence of the IBER, larger companies, in the interest of extending competitive advantage, may decline to participate in industry studies, thereby reducing the applicability of such studies and rendering the market less efficient.

Impact of non-renewal

Non-renewal would not mean that the currently exempted activities would be prohibited, but that agreements could be subject to individual scrutiny by competition authorities. The AAE believes that non-renewal would increase the likelihood of individual firms - especially owners of Big Data mentioned in the preceding paragraph - declining to participate in joint studies. Non-participation would at least make studies less representative and less valuable, ultimately inhibiting competition. Additionally, it would be more difficult for those participating to be assured as to the compliance of agreements with competition legislation if other players would challenge the legitimacy of such cooperation.

Conclusion

The AAE believes that this aspect of the IBER should be retained, particularly in the area of studies, compilations and tables relating to insurance risk factors.

Common coverage of certain types of risks (co/re insurance pools)

Insurance pools are generally set up for catastrophe-type risks which may be too substantial for any one insurer to cover alone or where there may be limited or no capacity in the reinsurance market for the risk concerned. They can also be used in areas of national interest, e.g. Flood Re in the UK, CatNat in France. There are a number of such entities established around Europe.

As well as facilitating coverage of risks which otherwise could not be covered, this has the benefit of providing diversification by spreading counterparty risk for insureds. The ability to establish pools is in the public interest and the AAE believes that it is appropriate that barriers to their establishment and proper functioning not be erected.

However, the AAE notes that there is not universal clarity as to what ventures technically constitute pools, (e.g. line slips) and that pools are subject to limitations which must be observed. This lack of clarity could in theory lead to anti-competitive outcomes though the AAE is not aware of such outcomes in practice.

Conclusion

The AAE believes that the ability to establish pools is in the public interest and that this should be facilitated by renewal of the exemption but with clarity as to

- definition of the type of entity which is exempted.
- applicable limits, e.g. in relation to the overall market.
- circumstances in which competition due diligence/self assessment are required.

Notes for editors

1. For further information please contact Ad Kok, Chief Executive (tel. +32 2 201 60 21), aamkok@actuary.eu
2. The Actuarial Association of Europe (AAE) was established in 1978 under the name *Groupe Consultatif* to represent actuarial associations in Europe. Its purpose is to provide advice and opinions to the various organisations of the European Union - the Commission, the Council of Ministers, the European Parliament, the European Supervisors and their committees – on actuarial issues in European legislation. The AAE currently has 37 member associations in 35 European countries, representing over 20,000 actuaries. Advice and comments provided by the AAE on behalf of the European actuarial profession are totally independent of industry interests.
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