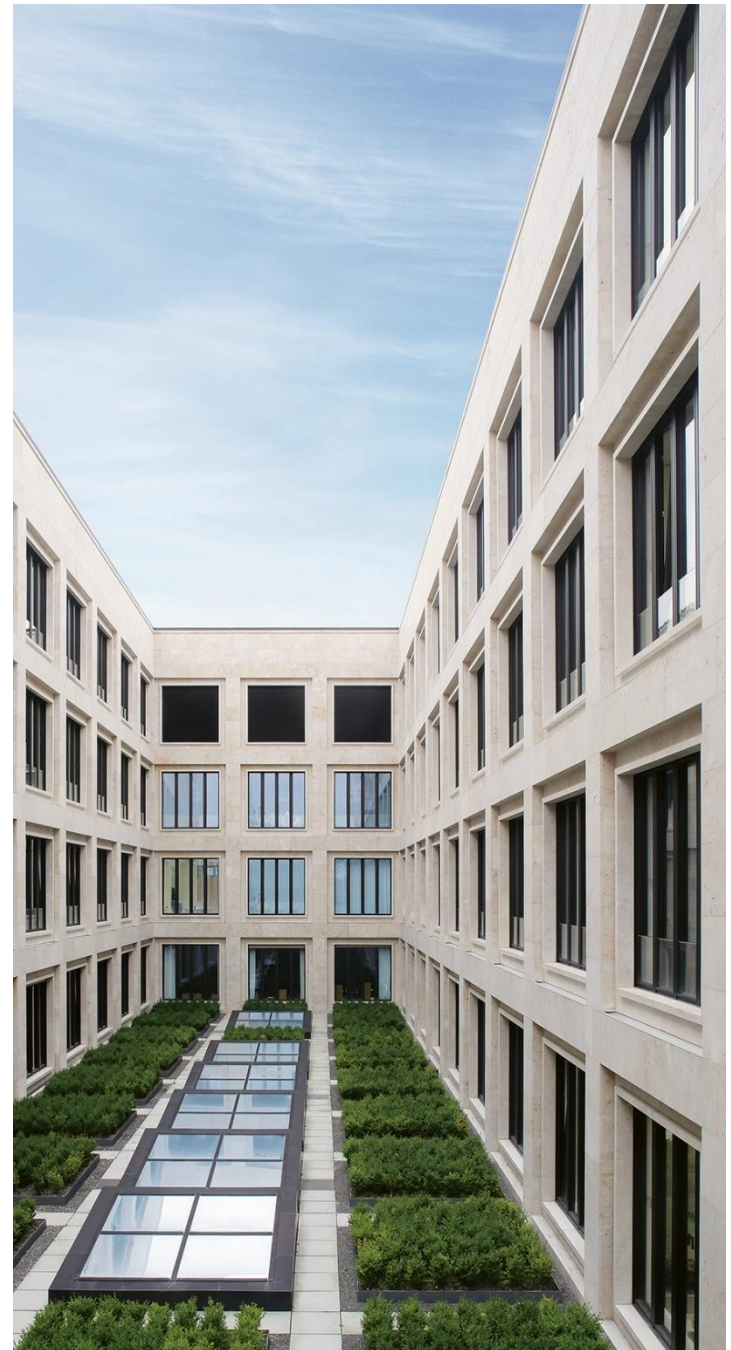


**Prof. Dr. Manfred Wandt**  
Goethe Universität, Frankfurt

## Transparency of insurance contract terms

AIDA XIVth World Congress  
Rome, 30.9.2014



# Agenda

1. Introduction
2. Requirement of a regulatory ex-ante approval of GCI
3. Mandatory contract terms
4. Formal requirements
5. Standard terms as part of the contract (esp. date of issuing the written GCI)
6. Interpretation of GCI
7. Requirements on transparency of GCI
8. Conclusion



# The driving forces behind the evolution of insurance law from a European perspective

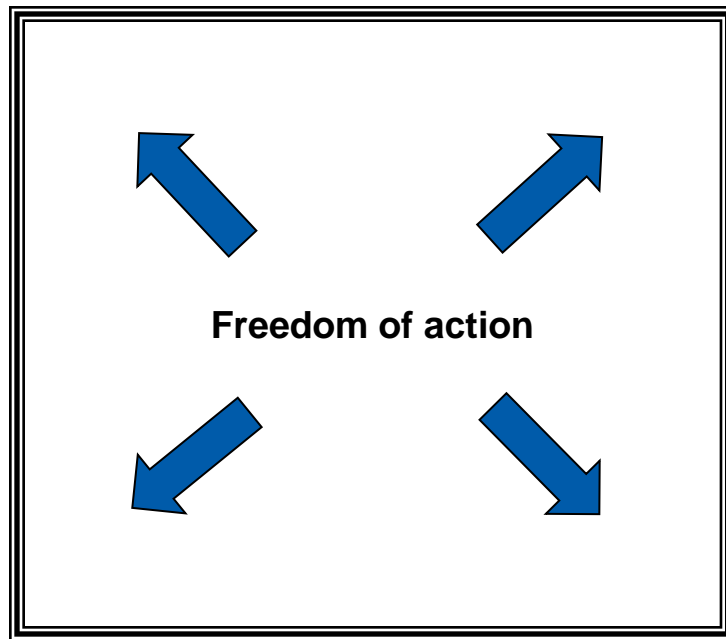
- Consumer protection (= insured protection)
- Information technology (transparency)
- Financial crises
- Globalization
- **EU internal insurance market** (completion and shaping)
  - Harmonization of law
  - Improving the Community lawmaking process
  - Creating a European financial supervisory architecture

# The need for insurance regulation (and consumer/insured protection)

- Insurance is a contract based upon money for a promise
- Longterm contracts
- cover will often serve an existential need of the insured
- mandatory insurances
- a complex and complicated legal product
- adhesion contracts
- standard terms define the main subject matter of the contract
- moral hazard

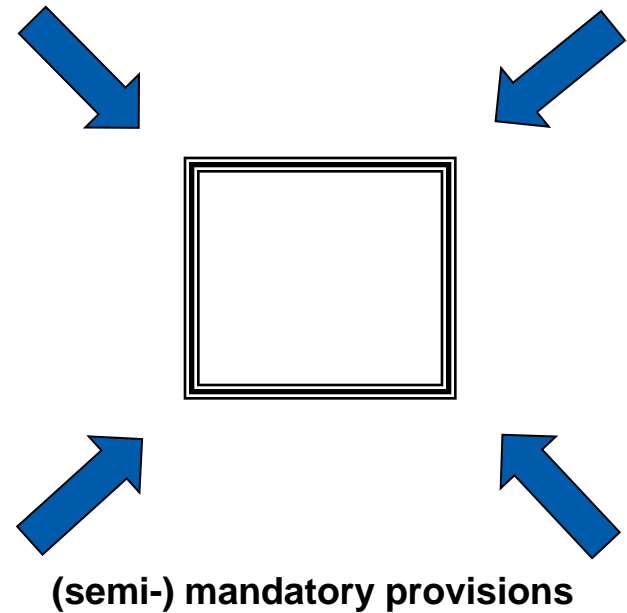
# Insurance contract law

## liberal legal system



## Welfare state

Consumer protection



# Insurance Supervision Law

- National law
- **E.g. German Insurance Supervisory Act 1901**
- in order to protect the insured
- but also to safeguard the functioning of the national insurance system

# The European dimension

## Single market in the EU

- **Treaty of Rome 1957: fundamental freedoms**
  - Freedom of establishment
  - Freedom to provide services
  - Free movement of capital
- **1973 – 1992 1st, 2nd and 3rd generation of EC directives**
  - Mainly harmonizing insurance supervisory law (+ company law)
  - Only minimum harmonisation of contract law in a very fragmentary way
  - a directive's proposal to harmonize the substantive private insurance law (1979) failed

## EU internal insurance market essential characteristics

- Principle of common authorization (so-called *single license*)
- Lead of home-country supervision
- minimum harmonization and mutual recognition of national supervisory systems
- elimination of preliminary authorization of the standard terms (in German: AVB) and tariffs (as a specific aspect of minimum harmonization)



### **European Court of Justice judgment of 4<sup>th</sup> December 1986:**

- insurance sector is a particularly sensitive area
- imperative reasons relating to the public interest which may justify **restrictions on the freedom to provide services**
- **provided, however, that**
  - the rules of the State of establishment are not adequate in order to achieve the necessary level of protection
  - and that the requirements of the State in which the service is provided do not exceed what is necessary in that respect.

## EU internal insurance market completion in 1994 (so called deregulation)

Third Directives in 1992 led to the **completion of the Single Market in the insurance sector in 1994**

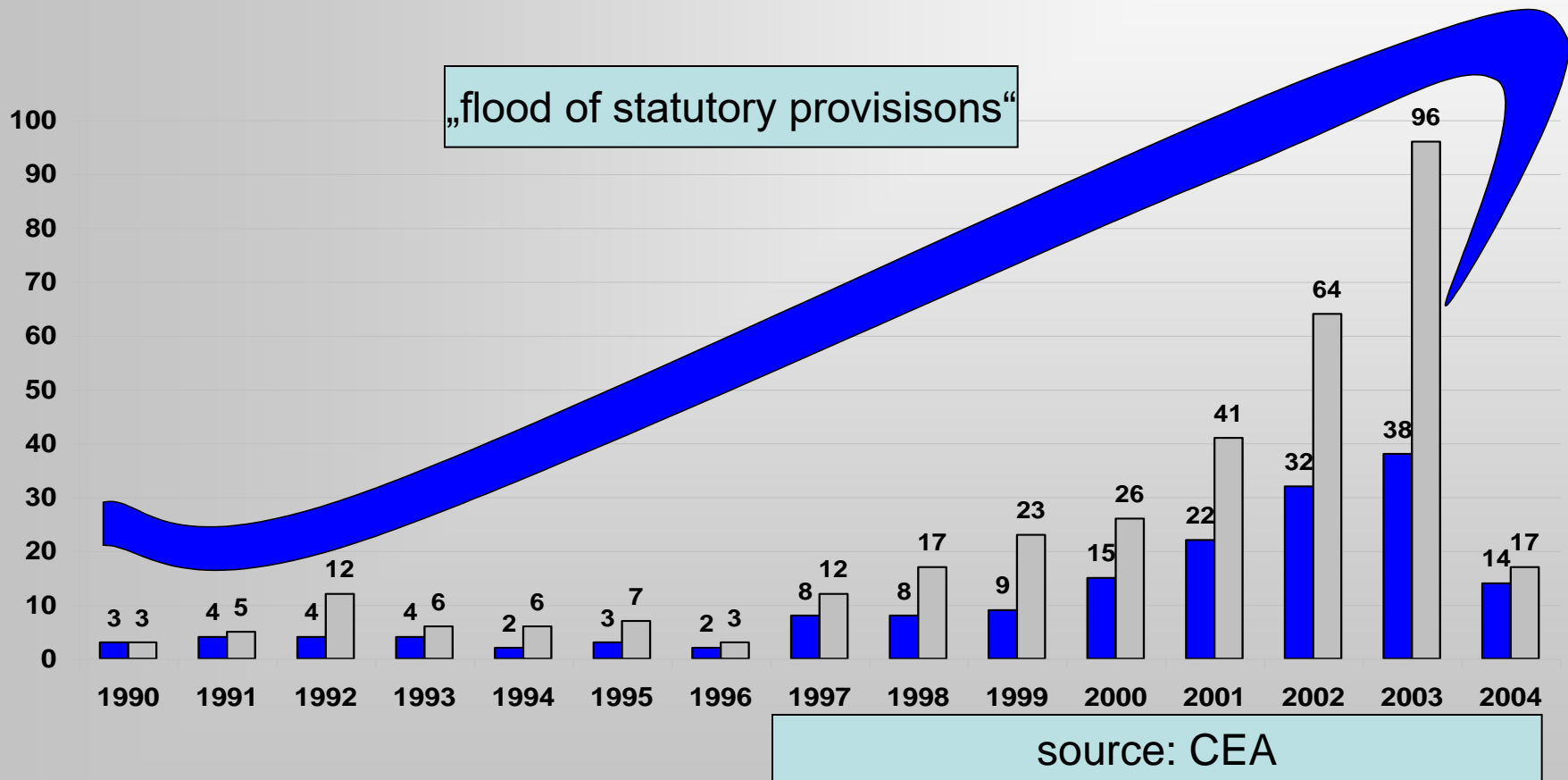
However, many obstacles to cross-border trade in insurance products

- 'knowing your customer' and understanding the true risk
- language,
- culture, including expectations of the local policyholder,
- the need for local claims handling,
- the tax and labour law environment,
- the legal, regulatory and supervisory environment, and cross-border redress options.

*“The establishment of the framework for the internal insurance market, in particular the realisation of the fundamental freedoms, proved itself to be extremely difficult”* (Helmut Müller, German Supervisory Authority, Legal Bases of the Internal Insurance Market in Europe, 20??)



**deregulation  $\neq$  simplification**  
**regulated liberalisation**



# The impact of financial crises

- 1990 – Japanese asset price bubble collapsed
- Early 1990s recession
- 1994–95 – 1994 Mexico – speculative attack and default on Mexican debt
- 1997–98 – 1997 Asian Financial Crisis – devaluations and banking crises
- 1998 Russian financial crisis
- 2000–2001 – 2001 Turkish economic crisis
- Early 2000s recession
- 1999-2002 – Argentine economic crisis
- 2001 – Bursting of dot-com bubble – speculations concerning internet companies
- 2007–08 – Global financial crisis
- 2010 European sovereign debt crisis

source: Wikipedia

# The impact of financial crises

The Lamfalussy report, published on 15 February 2001,

The **Lamfalussy process** was designed

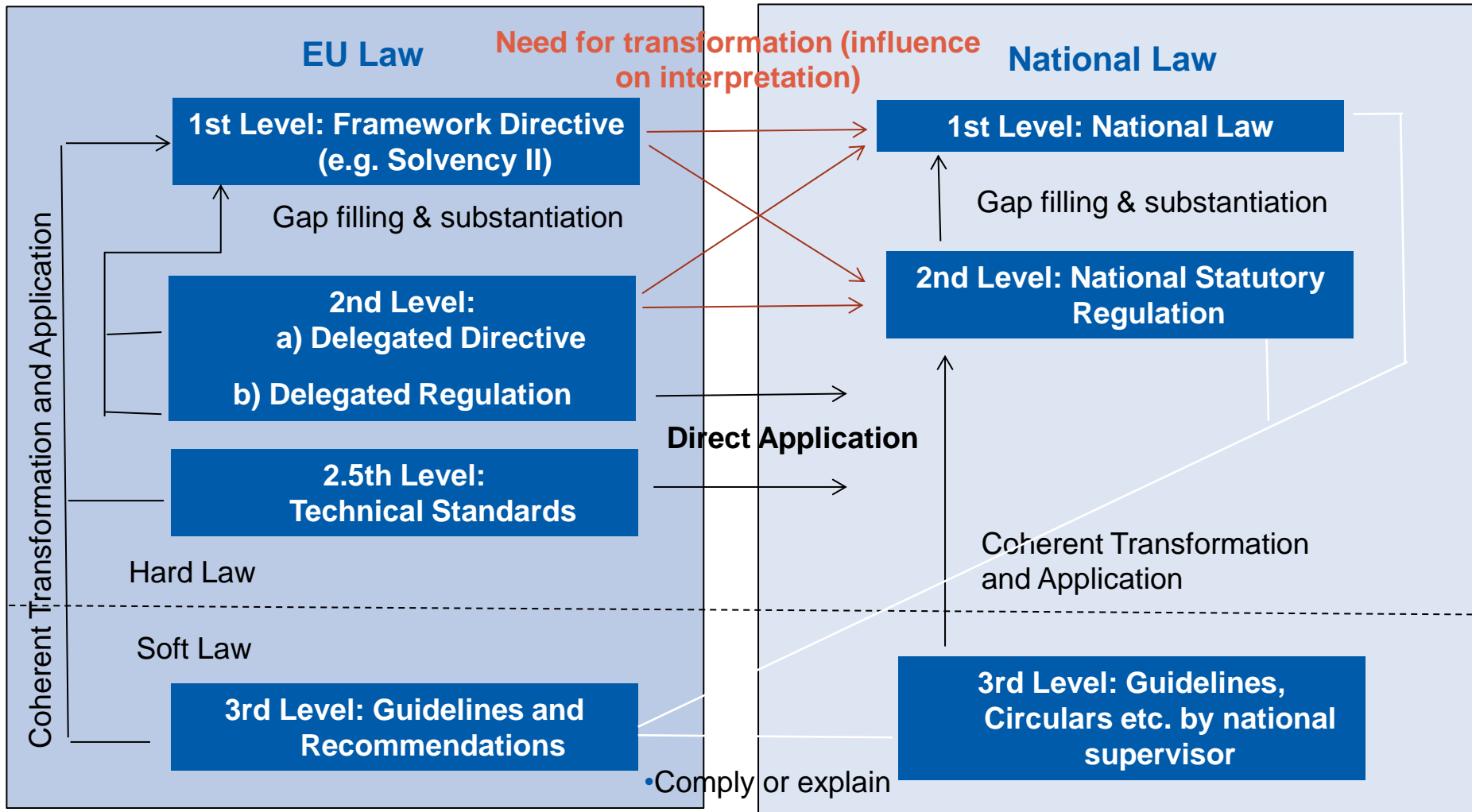
- to make **Community legislation on securities markets** more flexible, so that it can be agreed and adapted more quickly in response to innovation and technological change in financial markets;
- to allow the Institutions to benefit from the technical and regulatory expertise of European securities regulators and from better involvement of external stakeholders; and
- to focus more on even implementation and enforcement of Community law in the Member States.

Since 2002 the **Lamfalussy process is applied on insurance**

1. Need for Global Approach

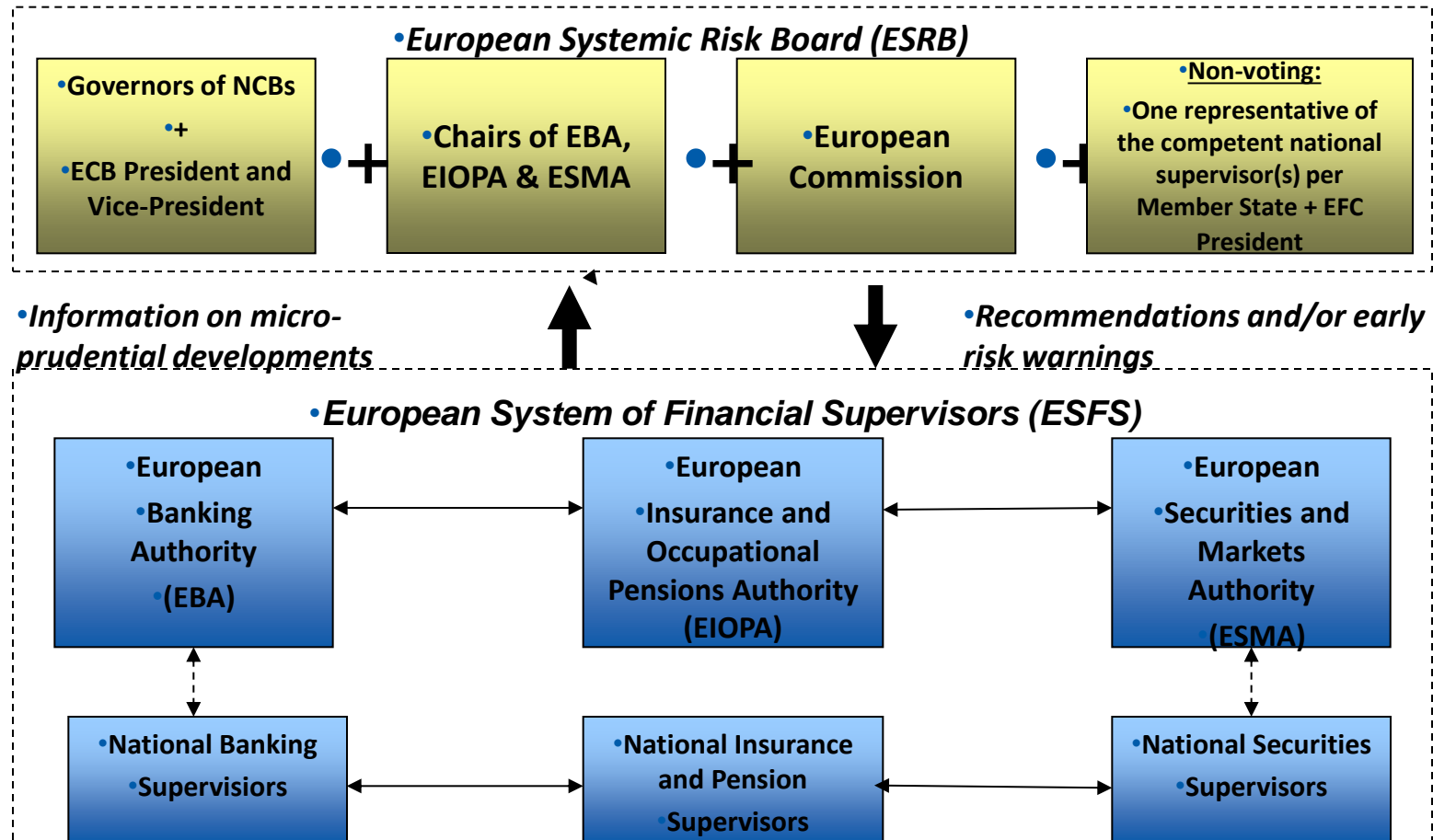
2. Global Architecture

3. Harmonisation of Regulation and Supervision



# New European financial supervisory architecture – de Larosière Report 2009

Quelle EU-Kommission



**“Müller Report” of 1997** assessed the European solvency systems:

- as on the whole satisfactory,
- however proposed a number of improvements.

**Financial Services Action Plan of the Commission of 1999**

**Revision of the solvency provisions** in two steps.

- **Solvency I:**

Modification of the provisions on the solvency margin in the existing Directives

- **Solvency II – project (since 1999/2001):**

comprehensive assessment of the elements affecting the financial position of an insurance undertaking



# Towards Solvency II

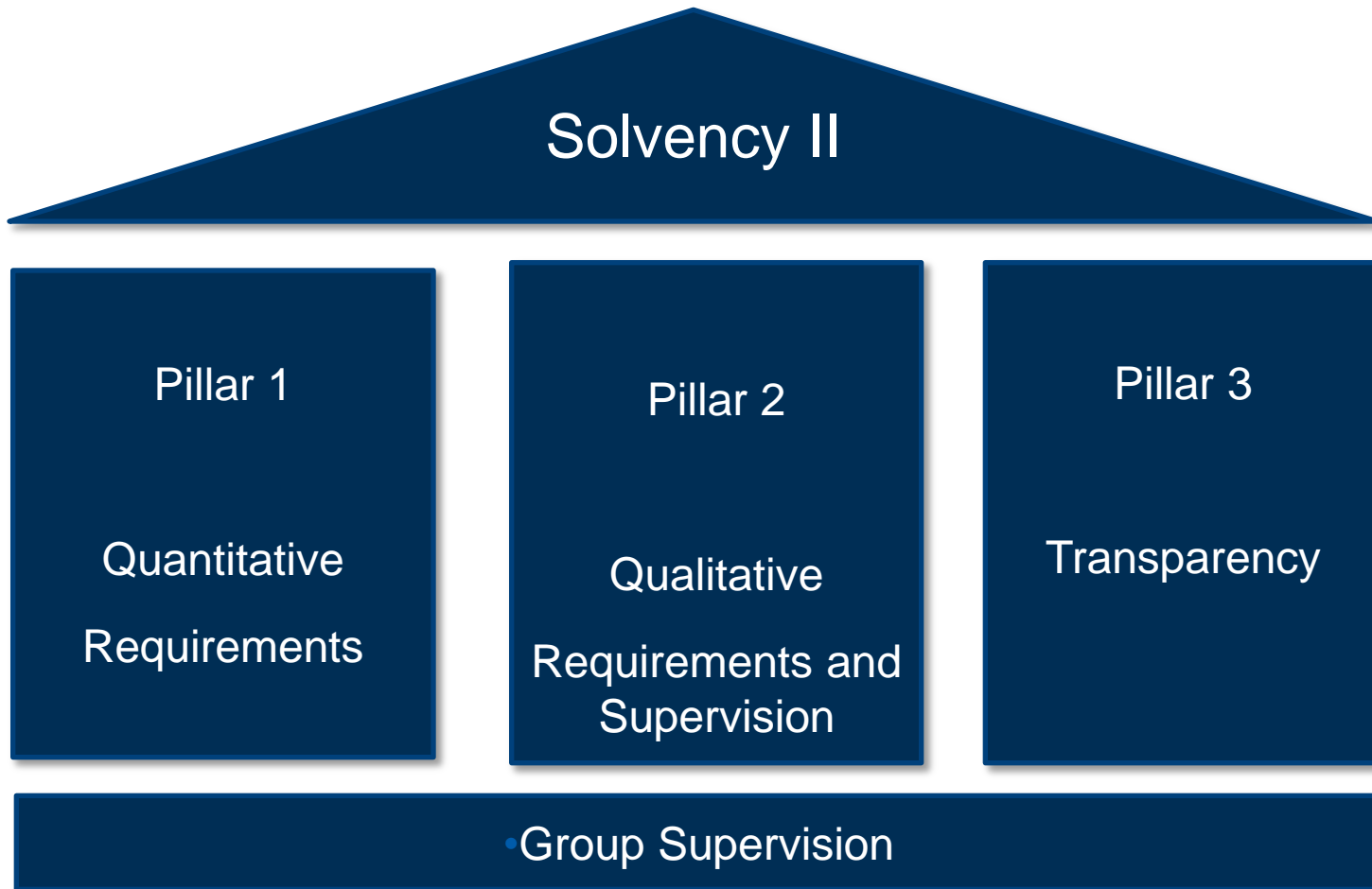
1999	EC Solvency II Review
2002	Sharma-Report/KPMG-Report
<b>2009</b>	<b>Solvency II Directive</b>

# Solvency I

Directive 2002/13/EC amending the solvency margin requirements for **non-life insurance** undertakings (OJ EC no L 77 of 20 March 2002, p. 17);

Consolidated Directive 2002/12/EC amending the solvency margin for **life insurance** undertakings (OJ no L 77 of 20 March 2002, p. 11)

# Solvency II – The New Regulation has the Purpose of Full-Harmonization



# The need for insurance regulation (and consumer/insured protection)

- Insurance is a contract based upon money for a promise
- Longterm contracts
- cover will often serve an existential need of the insured
- mandatory insurances
- a complex and complicated legal product
- adhesion contracts
- standard terms define the main subject matter of the contract
- moral hazard

## obstacles to cross-border trade in insurance products

- 'knowing your customer' and understanding the true risk
- language,
- culture, including expectations of the local policyholder,
- the need for local claims handling,
- the tax and labour law environment,
- the legal, regulatory and supervisory environment, and cross-border redress options.
- “The establishment of the framework for the internal insurance market, in particular the realisation of the fundamental freedoms, proved itself to be extremely difficult” (Helmut Müller, German Supervisory Authority, Legal Bases of the Internal Insurance Market in Europe, 19???)

## Political steps towards xxxx

- 1998, the European Council requested the Commission to develop a framework for measures to improve the Single Market for financial services,  
in view of the structural changes
  - in Europe: introduction of the Euro; enlargement of the Union
  - in the World market: increasing globalisation
- 1999 the Commission presented a Financial Services Action Plan

1. Need for Global Approach

2. Global Architecture

3. Harmonisation of Regulation and Supervision

Micro-Prudential Supervision

Joint Committee

EBA

EIOPA

ESMA

Supervisory Colleges

National Supervisory Authorities

Micro-prudential Information

Macro-prudential information as well as risk warnings and recommendations

Macro-Prudential Supervision

European Systemic Risk Board (ESRB)

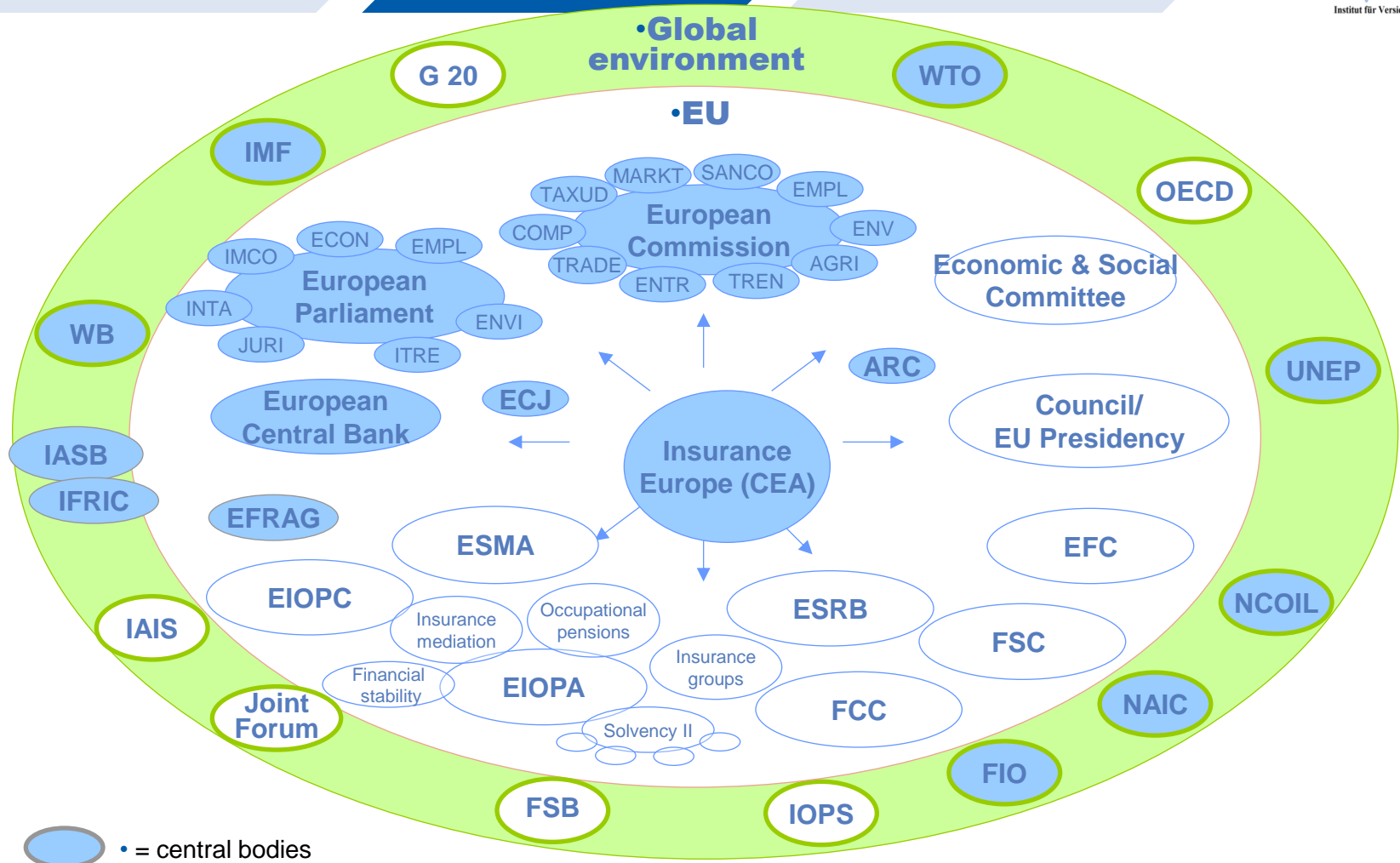
Warnings and recommendations to national Governments



1. Need for Global Approach

2. Global Architecture

3. Harmonisation of Regulation and Supervision



- = central bodies
- = representation of States

© Lloyd's



# EU-Legislation

## Insurance Supervisory Law



INSTITUT FÜR VERSICHERUNGSRECHT

1973 – 1992      1st, 2nd and 3rd generation directives   
**1994**      German **VAG-Amendment 1994 = Internal Insurance Market**

---

1997      Mueller-Report  
**2002**      **Solvency I-Directives**  **VAG-Amendment 2003**

---

1999      EC Solvency II Review  
2002      Sharma- & KPMG-Report  
**2009**      **Solvency II-Directive**  **VAG-Amendment draft 2012**

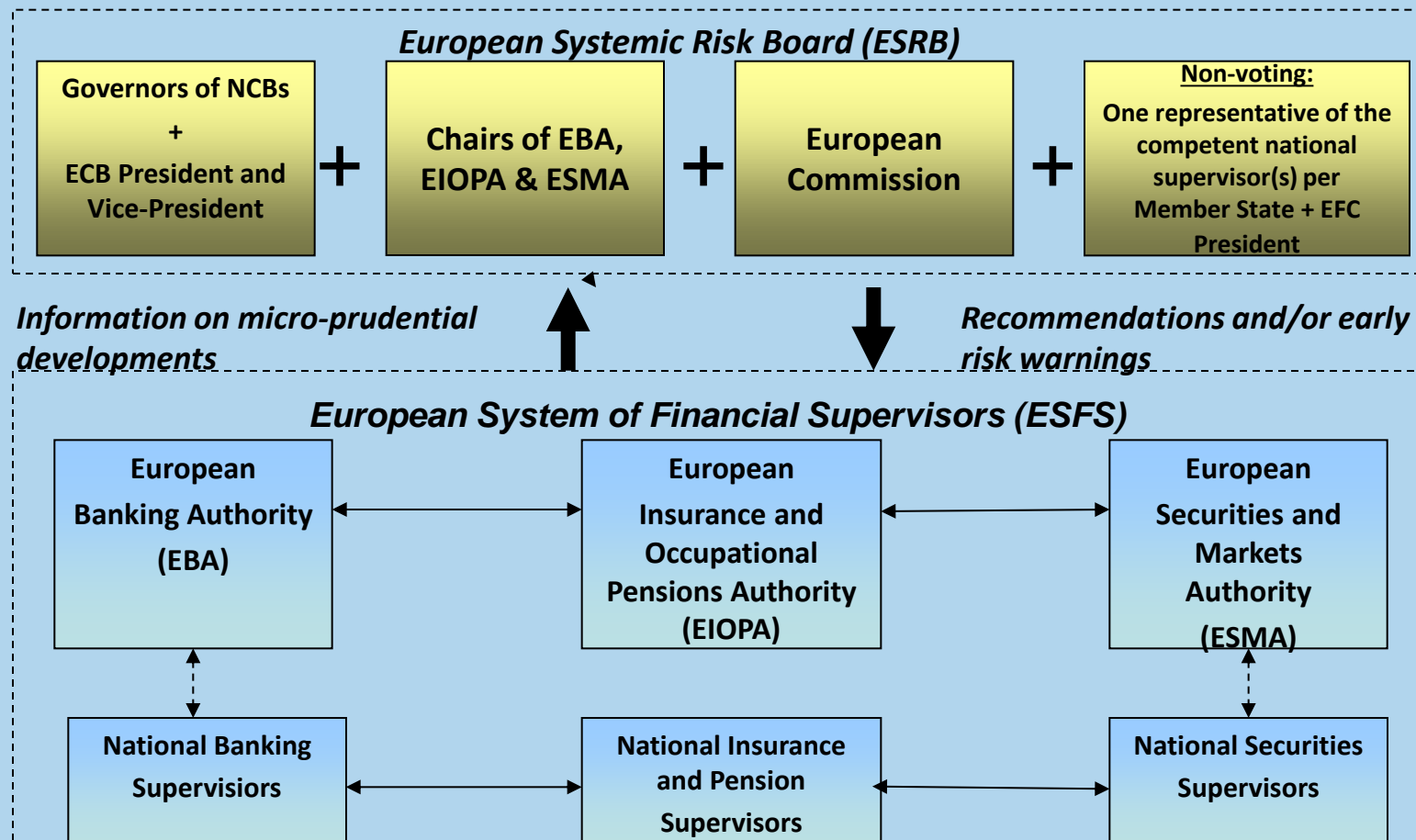
2012 ?      *Omnibus II-Directive (-Proposal)*  
                 *EP-Committee 21.3.2012: 1. Reading 17.4.2012*  
                 *(area-specific transitional provisions)*

# Neue europäische Finanzaufsichts- architektur - de Larosière Report 2009

Quelle EU-Kommission



INSTITUT FÜR VERSICHERUNGSRECHT



## Transparency of standard terms: economic importance and legal development

- » ***terms which have not been individually negotiated***« (PEICL) are the legal heart of an insurance contract within a b2c transaction
- **economic importance:** standard terms define the main subject matter of the contract (insured event / extent of coverage)
- transparency of GSI is an important aspect of strengthening consumer protection
  - EU: the standard of transparency has been continuously enlarged
  - common law countries:
    - general contract law applies;
    - specific rules are subject to the Insurance Supervision Law

# The overall legal framework concerning transparency of contract

Transparency of contract is mainly achieved by:

- pre-contractual duties of the insurer to give **information and advise**;
- **formal** requirements (constitutive for the conclusion of the contract);
- requirements on the **design** of information and of GCI;
- transparency requirements for the **content** of GCI;
- requirements for the **inclusion** of GCI in the contract (esp. date of issuing);
- duties to **inform** after the conclusion of the contract;
- the methods of **interpreting** GCI, esp.:
  - principle of restriction; *contra proferentem* rule
- **judicial control**

# Requirement of a regulatory ex-ante approval of GCI

- Worldwide, many countries: **regulatory ex-ante approval**
  - all GCI (e.g. Japan, Singapore, Turkey)
  - only GCI for **certain insurance contracts** (e.g. Switzerland: occupational pension schemes or supplementary health insurance)
- EU
  - requirement of ex-ante approval of GCI has been abolished since the deregulation of the insurance sector in 1994
  - Member States may impose an obligation on the insurer to submit the GCI for health insurance and compulsory insurances to the supervisory authority before using them

# Mandatory policy provisions / contract terms

- directly by mandatory provisions (e. g. Belgian law requires that life insurances must contain a large number of mandatory policy provisions)
- indirectly by mandatory provisions, according to which a definite legal consequence / a specific issue is not agreed upon, except it is clearly said in the contract / policy (e.g. France, Greece, Switzerland).
- insurance supervision law often provides for mandatory provisions on the content of general contract terms (e.g. Germany, Poland).

# Formal requirements

There are significant **differences in detail** between the national legal systems:

- only a few countries require a written form for the **conclusion of the contract** (e.g. Bulgaria; Hungary relating to life insurance contracts)
- some jurisdictions require written form only as **part of the law of evidence** (e.g. Austria, Belgium, France, Greece, Italy)
- some jurisdictions explicitly require that the **terms of consumer contracts** must be in writing (e.g. Brazil, South Korea, Turkey)
- **Article 2:301 PEICL (Manner of Conclusion)** expressly states that an insurance contract shall not be required to be concluded or evidenced in writing nor subject to any other requirement as to form. The contract may be proved by any means, including oral testimony.

# Standard terms as part of the contract (esp. date of issuing the written GCI)

- most countries require that GCI are issued **before** the conclusion of the contract
- some countries allow to transmit GCI **together with the policy** to the policyholder during **or after the conclusion of the contract**, esp.
  - in case of an oral agreement
  - waiver of pre-contractual information
  - waiver of issuing the GCI on concluding the contract
- **New Zealand**: it is assumed that both parties contract on the basis of the insurer's standard policy terms.
- **Taiwan**: a period of no less than 30 days must be given to consumers to review the contents of all terms and conditions before the conclusion of the contract. Otherwise GSI shall not be part of the contract, but consumers may propose that the terms and conditions make up the content of the standard contract.



# Standard terms as part of the contract (esp. date of issuing the written GCI)

## Unexpected terms:

- a surprising (unexpected) term do not form part of the contract (e.g. France, Germany, Hong Kong, Switzerland)
- Sec. 305c para. 1 German BGB
  - if the clause is unexpected from the point of view of a reasonable contractual partner, in particular with regard to all the circumstances attending the conclusion of the contract
  - According to case law: if the particular term is “hidden” between the terms and conditions

# Interpretation of GCI

Interpretation is generally based on the **intention of the contracting parties**. However:

- Most common-law jurisdictions start contractual interpretation from an objective point of view.
- In contrast, many EU member states follow a subjective standard of interpretation.
- It is rightly stated in scholarly literature that the results are regularly identical.
- standard terms are construed from the **view of an average policyholder** without any legal knowledge (e.g. Belgium, Germany, Greece).
  - Brazilian Consumer Code : **a prompt and easy understanding**
  - German case law: a policyholder who carefully reads and reasonably assesses GCI and considers the apparent contextual meaning
- ***contra proferentem* rule** applies almost worldwide for consumer contracts

# Judicial control of GCI

- **control of the material validity:**

- a particular term is ineffective if, contrary to the requirement of good faith, it causes a significant imbalance in the parties' rights and obligations arising under the contract, to the detriment of the consumer.

- **control of transparency**

- only minimum harmonization by the 1993 EC directive on unfair terms in consumer contracts

- **scope of judicial control**

- many countries: without restrictions
- English law exempts any description of the insured event and any exclusions
- German law exempts only the **core terms** of the contract without which the contract cannot be performed

# Statutory requirements concerning the language to be used

- contract terms must be drafted in the **official national language** (e.g. Greece, Hungary (life assurance contract), New Zealand, South Korea, Turkey).
  - **Turkey**: “Foreign words shall not be used in insurance contracts. Principally, the translation of foreign words shall be used as determined by the Turkish Language Institute.” (Article 11 para. 5 Insurance Activities Act)
  - **Taiwan**: „The wording in the sales material must contain Mandarin Chinese .... English terminologies and notes should be added if necessary.“ (Article 2 (3) of the Guidelines on Disclosing Information of Investment-linked Insurance)
- many countries alternatively permit the use of the **language agreed by the contracting parties** (e.g. Belgium, France, Germany, Taiwan)

# Statutory requirements concerning font-design

- **general provisions:** e.g. standard terms “to be printed in a clear and legible manner” (Greece) or “written ... with noticeable and readable characters” (Brazil).
- **specific provisions** for font design: **font size, bold print, block letters**
  - **Turkey:** consumer contracts must be written in bold print and not less than **12 points** (Consumer Protection Law).
  - **N.Y.:** policy ... not less than **10 point type** (Insurance LAW § 3102 (1) (E))
  - **France:** a policy clause that stipulates exclusions shall be valid only if it appears in **very clear print** (bold, block letters, etc) [Insurance Code]
  - **South Korea:** contract terms shall be written in Korean using plain and standardized terminology, indicating the material sections **marked in alternative colors, bold and large fonts** (Standard Terms Act)

# Statutory requirements concerning document- design

## **contract law:**

some laws provide for specific requirements concerning document-design.

**Greece:** GCI must be printed not only in a clear and legible manner but also **in a prominent position** on the contract document (Law 2251/1994)

## **Insurance supervision law, e. g.**

**Hungaria:** the format of documents (including GCI) must be **easy-to-read format** and **well structured**, and include a table of contents (nonbinding guideline of the Supervisory Authority on the consumer information to be provided by financial service providers).

**Hong Kong:** the policy / contract should be designed and presented with the aim of aiding comprehension by the individual private insured (Code of Conduct for Insurers).

## Comprehensibility: legal provisions and case law

- **Intelligibility of language, esp. terminology**
  - plain, intelligible language (e. g. Denmark, France, South Korea, South Africa, Turkey).
  - specific provisions on the intelligibility of exclusion clauses (e. g. Brazil: „clauses ... shall bear easily visible characters thus allowing a **prompt and easy understanding**)
- **Comprehensibility within the context**

It is only rarely that provisions explicitly address the contextual meaning.

- Israel: any condition or exclusion to the liability of the insurer shall be specified in the policy **close to the subject to which it relates** (or be indicated therein with special emphasis) [sec. 3 ICA] .

# *definiteness, unambiguity and completeness of GCI*

## ■ **Unambiguity**

- priority of the *contra proferentem* rule
- supplementary control of transparency
- An unambiguous rule may be considered unclear and *vice versa*.

**France:** exclusions must be “formal”, which means that they must be perfectly clear (Insurance Code)

**Switzerland:** any restriction must be expressed in “precise, unequivocal” language (ICA 1908)

## ■ **completeness**

- German Federal Court of Justice: an understandable term has to be complete insofar as it should reveal the economic disadvantages and burdens as far as it is reasonable.



Thank you for your attention

