Subscription Underwriting and Competition Law

The Business Insurance Sector Inquiry

In the final report from the EU Commission on its inquiry into the business insurance sector (published in September 2007), concerns were raised about the compatibility of certain subscription underwriting practices with EU competition law. The Commission challenged the insurance industry to reform these practices so as to avoid potential breaches of competition law. In response to that challenge, BIPAR, the representative body of European insurance intermediaries, adopted a series of principles that brokers are to observe in the subscription process, published at http://www.bipar.eu/en/library/principles.

This note provides guidance from the underwriters' perspective on competition law in relation to the placing process and supplements previous guidance issued by Lloyd's on 29 April 2008 as Market Bulletin Y4153.

The Legal Background

EU law contains a broad prohibition on agreements, arrangements and practices whether written or unwritten which have as their "object or effect" the "prevention, restriction or distortion" of competition. How this provision applies has been the subject of many decisions by the European Commission, national competition authorities and the European and national courts. Two of the most serious restrictions of competition which have been identified are:

- agreements between competitors on prices to be charged to third parties; and
- the sharing of competitively sensitive information between competitors relating to price or other terms of business.

The principles which underlie this prohibition are that it is for each competitor independently to determine its commercial position on any particular matter and anything which interferes with this independence may potentially restrict competition and therefore cause harm to consumers.

Principles to be observed in the underwriting process

Care therefore needs to be taken to ensure that the communication of information which occurs during the subscription process and the procedures for completing the slip do not fall foul of competition law.

1. *Underwriters should independently decide whether or not to participate in the insurance of individual risks presented to them by brokers and whether or not the proposed structure of underwriting is acceptable.*

   The BIPAR principles stress the role of the broker in presenting alternative potential underwriting structures to its client and also stress the ability of the client to choose the structure that best fulfils its needs. Underwriters should not obstruct this process and must independently analyse and decide on

whether or not they wish to underwrite the insurance risk in question using the method proposed by the broker. They must not coordinate this decision with other underwriters.

2. *Underwriters approached by brokers as potential leaders or as leaders of existing facilities should neither confer nor reach any agreement or understanding with other underwriters in deciding whether or not to underwrite and as regards the terms of any proposed underwriting, including premium.*

   Any prior consultation, collaboration or sharing of information between underwriters in these circumstances is very likely to be viewed as collusive. If so, it would be a serious breach of competition law.

3. *Underwriters approached by brokers to underwrite a risk at a particular premium as followers should neither confer with nor reach any agreement or understanding with any other underwriter in deciding whether or not to underwrite the risk in question or, where the decision is taken to underwrite the particular risk, as to the terms of the proposed underwriting, including premium.*

   While the Commission has indicated that it accepts the need for the leader's price to be revealed to the followers, the requirement of independent commercial behaviour prevents underwriters from sharing competitively sensitive information or reaching any agreements or understandings with other underwriters regarding the proposed underwriting.

4. *Underwriters should not, as a condition of any agreement to underwrite, require the upward alignment of premium nor should they initiate any such upward alignment should any subsequent underwriter require or secure a higher premium in order to participate in the underwriting.*

   The legal status of "best terms" requirements by individual underwriters remains unclear but the Commission is hostile to the use of such terms and the BIPAR principles also require brokers not to accept any term leading to the upward alignment of premium.

5. *Following underwriters should neither expect nor require brokers to pass on to them details of the terms (including premium) on which other following underwriters have underwritten or offered to underwrite the risk.*

   The exchange of competitively sensitive information directly between competing underwriters is not permissible. It is equally impermissible for brokers to be used by underwriters as a channel for the communication of information to other underwriters.

   This does not preclude a broker from revealing the terms of other underwriters (including premium) where the broker is using this as a bargaining device to obtain the best terms for its client.