LLOYD'S MARKET ASSOCIATION

COMPLIANCE WITH COMPETITION RULES

It is the policy of the LMA to comply with competition law at all times. Competition law prohibits agreements or understandings between organisations that have as their aim or effect the distortion or prevention of competition to a material degree. This guidance considers the competition law rules that are most relevant to the LMA, and outlines how the LMA seeks to ensure compliance in pursuing its activities.

The insurance sector has come under significant scrutiny in recent years, in part through the European Commission's business insurance sector review and in part because the Commission has been considering the future of the European legislation that for many years has exempted certain insurance market activities from the competition law prohibitions.

One exemption of particular relevance to the LMA concerned the production and distribution of standard or model wordings. The withdrawal of this exemption has required the LMA to review its approach to competition law compliance, both in relation to its wordings activities and more generally.

The review has led the LMA to adopt new model terms of reference for the many committees and panels in which the LMA and its members are involved. The LMA has also adopted new general guidance for its personnel and members relating to competition law compliance. This document sets out that guidance.

By accepting a place on any LMA or joint LMA/IUA committee or panel, a member agrees to comply with the terms of reference for the group in question and with this guidance. This guidance has been drawn up for the LMA by Barlow Lyde & Gilbert LLP. Any queries in relation to this guidance or any competition law issues that arise during the course of LMA committee, working group or panel meetings should be addressed to the LMA's Head of Legal and Compliance in the first instance.

COMPETITION LAW COMPLIANCE GUIDANCE

1. THE FRAMEWORK OF EU AND UK COMPETITION LAW

Competition law is aimed at preventing conduct which raises prices, limits the extent to which goods or services are produced or provided, or leads to the acquisition of market power which could have such consequences. This is achieved by controlling restrictive agreements, abuse of monopoly power and through imposing controls on mergers.

The area of competition law of most direct relevance to the LMA is the control of restrictive agreements. The specific provisions relating to restrictive agreements in the UK and the EU are set out as an Appendix to this note. The structure of competition law in the UK under the Competition Act 1998 broadly mirrors that applicable in the EU. One particular difference however is that EU law applies where an agreement has an "effect on trade between member states", a consideration which does not appear in UK law. Further, UK law provides that EU competition law principles (including case law and European Commission decisions) should be followed when considering activities undertaken and cases examined in the UK.

In one respect, UK law is significantly more punitive than EU law, namely in the application of criminal law to cartel activity. This is defined as covering the following arrangements between competitors where the activity is carried out dishonestly:

- price fixing;
- limiting the production or provision of goods or services;
- customer sharing; and
- bid rigging.

This note addresses both the prohibition on restrictive agreements and the cartel offence.

It is possible that certain activities carried on within the LMA may fall outside the law as being "de minimis", in other words, having only a minor market impact. However, this exception is notoriously difficult to apply, particularly because market definition is not straightforward. Accordingly, it is safer to proceed on the basis that competition law will apply, seeking specialist advice where it is anticipated that there is a prospect that the conduct may be viewed as having an insignificant impact on the market. This issue is considered further at paragraph 2.7.

2. COMPETITION LAW OF PARTICULAR RELEVANCE TO THE LMA AND ITS MEMBERS

2.1 RESTRICTIVE AGREEMENTS

Both UK and EU law may need to be considered as clearly many agreements between underwriters or involving the LMA could affect trade between member states. The law applies to agreements in any form and they do not have to be formally concluded. Oral agreements and informal understandings are therefore within the scope of the law.

The important question is what kinds of agreement are affected by these prohibitions. Generally, agreements between competitors which limit their freedom to compete individually (or are intended to achieve this) are the kinds of agreement that will fall within competition law. This is discussed in further detail in the Best Practice Guidelines for Members, set out below.

2.2 CARTELS

The cartel offence is particularly relevant to conduct by the LMA's members but the LMA could be found to have aided and abetted the commission of the offence by its members. This might occur, for example, if the LMA assisted its members in aligning their rates in respect of a particular type of risk, perhaps by collating and circulating information in respect of each member's own rates.

2.3 INFORMATION EXCHANGE

Other activities may have a more indirect effect on competition, such as the exchange of commercially sensitive information. For competition to work effectively, each competitor must independently determine the way in which they will conduct themselves on the market. The exchange of commercially sensitive information is considered to materially reduce uncertainty as to the behaviour of competitors and thereby compromises such independence. For these purposes, information is viewed as commercially sensitive if it is of such a nature that one would not normally wish to disclose it to a competitor. Trade bodies are frequently the place where such exchanges of information have in the past occurred. On the other hand, trade bodies are often a valuable source of industry information and the law makes specific provision for such information gathering to occur. In order for this practice to comply with competition law, the data needs to be aggregated and anonymised, so that the information relating to any one undertaking remains hidden from competitors. In addition, the more historic the data that is disseminated, the less likely it is to affect the conduct of competitors and therefore amount to an infringement of competition law.

2.4 MEMBERSHIP CRITERIA

While the rules of trade associations are unlikely directly to restrict competition, they may well do so indirectly where, for example, they exclude certain otherwise qualified businesses from membership. Non-admission to the "club" or the threat of expulsion could be a means of reinforcing certain trading behaviour such as avoiding significant rate cuts. For this reason, EU competition law has intervened on a number of occasions to ensure that where trade associations represent a significant number of industry members, they must adhere to various criteria so as to ensure that membership applications are considered on the basis of objectively justified criteria.

Guidance can be drawn in this area from the recent investigation by the European Commission of the International Association of Classification Societies ("**IACS**"). The essence of the Commission's concern was that the IACS members collectively enjoyed an extremely powerful market position and that through a number of IACS decisions, providers of similar services that were not IACS members suffered considerable competitive disadvantages.

The Commission objected in particular to decisions concerning the criteria used to establish IACS' membership (and the way these were applied in practice), in that they did not meet the requirements of being objective, transparent and non-discriminatory. The Commission also objected to the limited transparency of IACS resolutions, and to the discriminatory access it offered to technical background documents.

In order to meet the Commission's objections, IACS was obliged to reform its membership criteria, and to agree to apply them in a uniform and non-discriminatory manner. Further, classification societies that are non-IACS members would nevertheless be permitted to participate in IACS' technical working groups. All current and future IACS resolutions, together with their related background documents will also be made available to non-members, and an independent appeal board will be established to deal with any disputes that arise concerning these issues.

2.5 THE INSURANCE BLOCK EXEMPTION REGULATION ("IBER")

As stated above, the European Commission has withdrawn the legislation relating to the establishment of standard policy conditions. This has been a key aspect of the activities of working groups and is therefore a significant development. However, the fact that the exemption has been removed does not mean these activities are no longer allowed.

Advice taken by the LMA indicates that although the change will remove a degree of legal certainty, the activity can continue provided a number of safeguards remain in place. Specific guidance for wordings groups has therefore been put in place.

2.6 PENALTIES

Penalties for the infringement of either EU or UK competition law include:

- fines on individuals and possible imprisonment in respect of cartel arrangements;
- unenforceable contracts – an agreement that breaches competition law will be unenforceable in the courts;
- investigation and prohibition – even if no fines are imposed, the waste of management time and damage to reputation resulting from a breach of the law and the ensuing investigation can harm an organisation;
- third party suits for injunction and damages – such claims are becoming more frequent and raise the prospect of significant liabilities for infringers;
- fines up to 10% of world-wide group wide turnover even where the agreement does not amount to a cartel.

2.7 AGREEMENTS OF MINOR IMPORTANCE

Although competition law imposes strict controls on restrictive agreements, the law recognises that some practices, whilst in contravention of the law, are too

small to have a detrimental effect on the wider economy. As a result, if the parties to an arrangement that would otherwise be subject to competition law fall below certain thresholds, most (but not all!) anti-competitive activities they engage in will be deemed to fall outside the scope of competition law. These exclusions do not apply to the criminal cartel offence so that, for example, even a minor example of price fixing between competitors can amount to a criminal offence.

The market share thresholds in both UK and EU law are:

- 10% for agreements between competitors; and
- 15% for agreements between non-competitors.

Some things however are never regarded as insignificant in competition law terms, e.g. price fixing arrangements between competitors.

In addition, the exchange of commercially sensitive information that could facilitate the conclusion of the most damaging anti-competitive agreements (e.g. price fixing) will inevitably be seen as being anti-competitive (regardless of the scale of the activity).

BEST PRACTICE GUIDELINES FOR LMA CHAIRMEN AND SECRETARIAT

Meetings at which the LMA is present or which are organised by the LMA should not be the occasion for exchanges of confidential information or the conclusion of prohibited agreements. This does not prevent typical industry association activities of gathering and disseminating information but if this is to occur in relation to commercially sensitive information, the LMA must ensure that:

- information is handled only by the Secretariat and not individual members and that individual members do not have access to it;
- information, once collated, is in anonymised form which does not permit individual members to be identified; and
- analysis and recommendations accompanying the data are kept to a minimum. The concern here is that such additional wording may be seen as some form of recommendation from the LMA encouraging particular common responses from members. In other words, the information or statistics should be left to "speak for themselves".

Where policy conditions are under discussion the Chairman and Secretary should consult and comply with the Best Practice Guidelines for Wording Groups set out below.

Should an infringement of competition law occur or appear likely to occur at a meeting, the Chairman and/or Secretary present must remind members of the law and, if necessary, terminate the meeting. If members are insistent that they wish to consider the issue in question, any LMA representatives present must withdraw from the meeting and ensure that this withdrawal is minuted.

It is prudent for an agenda to be circulated in advance and for minutes to be kept of all meetings where the LMA is present. This encourages members to keep the discussions focused on areas approved by the LMA, and provides evidence that meetings are not being used as a forum for unlawful agreements or information exchanges.

Membership of the LMA and its committees or panels, and their operation should be determined in accordance with the relevant Terms of Reference for the group in question. The Chairman and Secretary should also have regard to their responsibilities for the conduct of meetings as set out in those Terms of Reference.

It is crucial that membership of the LMA and its committees or panels are determined on the basis of fair, transparent and objectively justifiable grounds, and the Chairman and Secretary should have regard to these general principles at all times.

BEST PRACTICE GUIDELINES FOR MEMBERS

It is vital that the compliance of the LMA is not compromised through the activities of its members, and consequently this section provides guidance on high risk areas which members should avoid. This section identifies those areas of competition law that may be relevant. It focuses particularly on the activities of underwriters given that their activities would seem to pose the greatest risk from the competition law perspective.

Some agreements that members enter into are unlikely to affect competition between them. For example, an agreement to comply with certain technical requirements when exchanging claims data would be unlikely to concern the competition authorities.

On the other hand, agreements that might directly affect competition would include agreements between members:

- not to deal with a particular undertaking such as a broker;
- as to premiums or any other element of price such as surcharges that each will charge;
- to deal with other parties, e.g. loss adjusters, only on certain conditions; and
- to underwrite only on specific terms.

In addition, members should be aware that the cartel offence may be relevant to their activities in certain circumstances. An example would be an agreement between underwriters such that one underwriter agrees not to make an offer to participate in a particular insurance programme, perhaps on the basis that the other underwriter will in turn not make an offer in respect of a future opportunity. If this arrangement is kept hidden from the broker/ insured, this could amount to bid rigging for the purposes of the legislation.

Information exchange is another area in which members should exercise caution. The law prohibits exchanges of commercially sensitive information between competing undertakings. Consequently, exchanging information as to the rates underwriters have each recently quoted for particular risks, or as to the rates for risks which are currently being underwritten, would infringe competition law. This prohibition applies irrespective of whether the exchange of information leads to actual price co-ordination between the underwriters in question.

As a result of the above, members should be aware of the implications of attending meetings where information is to be exchanged. Even though it is the policy of the LMA to avoid the discussion of commercially sensitive information, it is always possible for a member who has not fully understood the requirements of competition law to stray into higher risk areas. A typical case is where leading competitors in a particular class discuss trends in relation to rates and conclude, even in non-specific terms, that rates need to increase. If such exchanges of information take place, fellow members (in addition to the Chairman and Secretary) should make them aware that the discussion risks infringing competition law and should end immediately. Members should make sure their objection is noted in the minutes, and if the discussion continues they should remove themselves from the meeting. It will not be sufficient to continue participation at the meeting and remain silent.

BEST PRACTICE GUIDELINES FOR WORDING GROUPS

Until recently, the European Commission exempted the establishment of common, non-binding standard policy conditions in the insurance sector from the full application of competition law by virtue of the IBER. This aspect of the IBER was not renewed when it expired on 31 March 2010.

However, wording groups can continue to carry out these activities provided certain high risk areas are avoided and a number of safeguards remain in place. Such standard clauses must not however seek to exclude the possibility of variants. Individual underwriters are free to accept, reject or vary the terms of model wordings, and must avoid any agreement or understanding as to the use to be made of model wordings in practice.

Equally, no panel should impose the use of wordings or clauses, nor should it recommend their use. Any publication of wordings and clauses should expressly state that they are not binding and that all Members are free to offer different policy wordings and clauses to their customers. This has been the LMA's standard practice for many years.

Where proposals are expected to be controversial and where there are clearly identifiable representatives of insureds who will be affected by proposed wordings, consideration should be given to consulting potentially affected industry participants on proposed wordings and clauses prior to their official publication, and offering them the opportunity to comment. Even where no specific consultation is carried out, it may be helpful for wording groups to make wordings, clauses (and consultation drafts of these if this approach is adopted), and minutes of meetings available on the LMA's website.

Wording groups should be transparent, allowing members and experts to discuss proposed drafting from a technical or legal perspective in an open and constructive manner.

Wording groups will only propose drafts or publish wordings or clauses that comply with competition law. For the avoidance of doubt, wording groups will not be involved in the drafting of clauses which the European Commission did not consider capable of exemption under the IBER. Consequently wording groups will not produce clauses which:

1 contain any indication of the level of commercial premiums;

2 indicate the amount of cover or the part which the policy holder must pay himself (the "excess");

3 impose comprehensive cover including risks to which a significant number of policyholders are not simultaneously exposed;

4 allow the insurer to maintain the policy in the event that he cancels part of the cover, increases the premium without the risk or the scope of the cover being changed (without prejudice to indexation clauses), or otherwise alters the policy conditions without the express consent of the policy-holder;

5 allow the insurer to modify the term of the policy without the express consent of the policyholder;

6 impose on the policyholder in the non-life assurance sector a contract period of more than three years;

7 impose a renewal period of more than one year where the policy is automatically renewed unless notice is given upon the expiry of a given period;

8 require the policyholder to agree to the reinstatement of a policy which has been suspended on account of the disappearance of the insured risk, if he is once again exposed to a risk of the same nature;

9 require the policyholder to obtain cover from the same insurer for different risks;

10 require the policyholder, in the event of a disposal of the object of insurance, to make the acquirer take over the insurance policy; or

11 exclude or limit the cover of a risk if the policyholder uses security devices, or installing or maintenance undertakings, which are not approved in accordance with the relevant specifications agreed by an association or associations of insurers in one or several other Member States or at the European level.

Further, the Panel will only propose drafts or publish wordings that comply with the BIPAR (European Federation of Insurance Intermediaries) high level principles for placement of a risk with multiple insurers. In particular, the Panel will not draft "best terms and conditions" clauses or clauses which have the same effect. The European Commission has defined such clauses as:

"any stipulation, whether written or oral, introduced at any stage of the negotiation of a reinsurance contract, by means of which a (re)insurer A obtains, seeks to obtain or acquires the right, under certain circumstances, to obtain an alignment of its proposed or agreed terms and conditions, in particular the premium, to the terms and conditions ultimately obtained by any other (re)insurer B participating in (re)insuring the same (re)insured as A, in the event that the latter terms are more favourable to the (re)insurer, than the terms and conditions which A offered or subsequently agreed."

The Panel will comply at all times with Lloyd's guidance with regard to these principles, which can be found at http://www.lloyds.com/NR/rdonlyres/A5D0502F-F64D-48A9-9E91-7BC20EB14647/0/Y4153.pdf.

APPENDIX

Article 101 of the Treaty on the Functioning of the European Union states:

(1) The following shall be prohibited as incompatible with the common market: all agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the common market, and in particular those which –

(a) directly or indirectly fix purchase or selling prices or any other trading conditions;

(b) limit or control production, markets, technical development, or investment;

(c) share markets or sources of supply;

(d) apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;

(e) make the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts.

2. Any agreements or decisions prohibited pursuant to this Article shall be automatically void.

The "Chapter I Prohibition" set out in section 2 of the Competition Act 1998 states:

(1) Subject to sub-section 3, agreements between undertakings, decisions by associations of undertakings or concerted practices which –

(a) may affect trade within the United Kingdom, and

(b) have as their object or effect the prevention, restriction or distortion of competition within the United Kingdom,

are prohibited unless they are exempt in accordance with the provisions of this Part.

(2) Sub-section (1) applies, in particular, to agreements, decisions or practices which –

(a) directly or indirectly fix purchase or selling prices or any other trading conditions;

(b) limit or control production, markets, technical development or investment;

(c) share markets or sources of supply;

(d) apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;

(e) make the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts.

(3) Subsection (1) applies only if the agreement, decision or practice is, or is intended to be, implemented in the United Kingdom.

Section 188 of the Enterprise Act 2003 states:

(1) An individual is guilty of an offence if he dishonestly agrees with one or more other persons to make or implement, or to cause to be made or implemented, arrangements of the following kind relating to at least two undertakings (A and B).

(2) The arrangements must be ones which, if operating as the parties to the agreement intend, would:-

(a) directly or indirectly fix a price for the supply by A in the United Kingdom (otherwise than to B) of a product or service,

(b) limit or prevent supply by A in the United Kingdom of a product or service,

(c) limit or prevent production by A in the United Kingdom of a product,

(d) divide between A and B the supply in the United Kingdom of a product or service to a customer or customers,

(e) divide between A and B customers for the supply in the United Kingdom of a product or service, or

(f) be bid-rigging arrangements.

(3) Unless subsection (2)(d), (e) or (f) applies, the arrangements must also be ones which, if operating as the parties to the agreement intend, would:-

(a) directly or indirectly fix a price for the supply by B in the United Kingdom (otherwise than to A) of a product or service,

(b) limit or prevent supply by B in the United Kingdom of a product or service, or

(c) limit or prevent production by B in the United Kingdom of a product.

(4) *In subsections (2)(a) to (d) and (3), references to supply or production are to supply or production in the appropriate circumstances (for which see section 189).*

(5) *"Bid-rigging arrangements" are arrangements under which, in response to a request for bids for the supply of a product or service in the United Kingdom, or for the production of a product in the United Kingdom:-*

(a) *A but not B may make a bid, or*

(b) *A and B may each make a bid but, in one case or both, only a bid arrived at in accordance with the arrangements.*

(6) *But arrangements are not bid-rigging arrangements if, under them, the person requesting bids would be informed of them at or before the time when a bid is made.*

(7) *"Undertaking" has the same meaning as in Part 1 of the 1998 Act.*