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THE CREATION OF THE EUROPEAN INSURANCE MARKET 
AND ITS IMPACT UPON JAPAN

JUN YOKOYAMA

Last year, the European Council successively adopted two directives in respect of 
insurance, that is, the Third Non-Life Insurance Directive and the Third Life Insurance 
Directive. They are designed to accomplish the creation of an internal insurance market 
within the EC. It will lead to the stimulation of competition throughout the EC and will 
make the European insurance market almost as sizeable as the Japanese one. The study 
of the EC insurance law seems to have much significance to us. At least from the regulatory 
point of view, the single insurance market undoubtedly becomes more attractive to the 
non-EC interests including our business circle.

The EC insurance law consists of a complex series of Directives. The time allows me 
to give only its very brief and bold outline from the following three points of view.

The first point is that the EC insurance law may provide something that we should 
learn, when we have to deal with legal problems relating to insurance, either de lege lata 
or de lege ferenda. I have to point out that, in the light of the particular nature of insurance, 
the interests of free supply of insurance services must be necessarily balanced against those 
of consumer protection. I would say that the rules contained in a series of Directives show 
a way to balance those interests with each other, both in the sphere of administrative law 
and in that of private law.

Secondly, I should remind you that the Uruguay Round of the GATT negotiations 
include insurance services. The economic integration on the regional basis such as the 
EC leads to the preferential treatment granted to the member states to the integration. We 
have to see how it may be reconciled with the principle of Most-Favoured-Nation Treatment 
as enunciated in the General Agreement on Trade in Services.

The third point is that the EC insurance law may be a foreign pressure, what we call 'Gaiatsu'. We should refer to a speech delivered by Sir Leon Brittan in Japan three years 
ago. He was, at that time, the United Kingdom's senior EC Commissioner with respon-
sibility for financial services including insurance. In this speech, he said, 'Le me make 
this absolutely clear: Where a third country's financial market is open to the Community 
financial institutions, that country's financial institutions will in turn be given full access 
to the Community.' The EC Council Directives now contain the so-called reciprocity 
clause. The past experience shows that our domestic institutions or laws have been improved in the form of a concession to foreign pressure. It is plausible that the reciprocity 
clause will give an enormous impetus to the movement towards the reform of our insurance 
law.
I. The Three Generations of Directives

Each of the Directives as mentioned at the outset, that is, the Third Non-Life Insurance Directives and the Third Life Insurance Directive, has its own two predecessor. Thus, it is said that a legislative work in the field of insurance consists of the three generations of the directives. As compared with the banking section in which only two Directives have been adopted, the rules set out in the insurance section seem to be more complicated. The freedom of establishment (as laid down in Articles 52–58, Treaty of Rome) and the freedom to provide services (as laid down in Articles 59–66) would only be obtained if the disparity in the laws of the Member States were reduced by the coordination and harmonization. However, it does not seem to have been easy in this field, principally because the disparity of the rules of the Member States are apparently so great in respect of the consumer protection.¹

For the sake of convenience, I would like to divide the rules contained in the Directives of the three generations into two, that is, the rules of administrative law and those of private law.

A. Administrative Law

The Directives of the three generations are mainly concerned with the harmonization of prudential control exercised by the supervisory authorities of the Member States, particularly with respect of solvency rules to the insurance undertaking.

1. The First Generation

The First Non-Life Insurance Directive and the First Life Insurance Directive were adopted in 1973 and 1979, respectively.

Broadly speaking, these Directives purport to set out the minimum requirements according to which an undertaking is to obtain authorization to open a head office in a Member State or to set up branches in other Member States. They enabled EC insurance companies, including subsidiaries owned by non-EC companies, to set up an establishment in any one or more of the 12 Member States. It succeeded in introducing the common system of solvency margins throughout the EC.

However, apart from this, the Directives of the first generation, it is said, do not represent a major breakthrough towards a genuine single market.² Authorization is almost subject to the regulatory rules of each Member State where an establishment will be.

2. The Second Generation

While the directives of the first generation were concerned with the establishment of the insurer, those of the second generation deal with the cross-border insurance services.

¹ See, Ottow, An Internal Insurance Market before the Turn of the Century, CML Rev, p. 515.
a. The Second Non-Life Insurance Directive

The Second Non-Life Insurance Directive was adopted on June 22, 1988. This Directive enables an insurer to cover risks in another Member State without being established there. This cross-border insurance services can be done either from its head office or from a branch.

It does not necessarily mean, however, that, once an authorization is provided by the country in which the head office of the insurer is established (hereafter called the home country), it is recognized by all the other Member States. Such a home country control or single licence system is not achieved to the fullest extent.

Subject to the limits laid down by the European Court of Justice in 1986, a Member State where the risk is situated (hereafter called the host country) is still empowered to approve the policy conditions, premium rates and documents to be used with policy-holders.

It is to be noted, further, that, instead of harmonizing the Member States' prudential rules designed to protect the interests of the policy-holders, the Directive makes a distinction between 'large risks' and 'mass risks' in terms of either the nature of the risk or the nature of the risk and the size of the policy-holder. The home country control applies only to 'large risks' in respect to which the consumer protection has less importance, whereas the host country may make the cover of 'mass risks' subject to its administrative authorization by reason of consumer protection. Control of technical reserves for mass risks remains a matter of the host country.

We should add that the principle of 'cumul' must be allowed for large risks, but that it need not be allowed in respect of mass risks. For example, an insurer with its head office in London and a branch in Paris may cover a large risk situated in France from either its London head office on a cross-border service basis or directly from its Paris branch.3 On the other hand, the anticumul principle may prevail with respect to mass risks: a Member State in which an insurer is established may force an insurer to cover mass risks only through its local branch. If the risk is a mass risk in the example I have just mentioned, the insurer may cover a mass risk only through its branch in Paris.

Nevertheless, the Second Non-life Insurance Directive is said to make a major breakthrough towards a genuine common market in insurance. As far as the large risks are concerned, the home country control or the single licence system enables industrial or commercial interests to insure their risks spread throughout the EC under a single contract.4

b. The Second Life Insurance Directive

The Second Life Directive was adopted on November 8, 1990. This Directive makes a distinction between policy-holders who take the initiative in entering into a commitment in another Member State and the other policy-holders.

The consumer acting on his own initiative is regarded as having abandoned the benefit of consumer protection in the host country, so that the insurer is allowed to provide cross-border services without the need of an authorization of the host Member State. The principle of cumul is also applicable in this 'own initiative' case.

In any other circumstances, that is, where the policy-holder does not take the initiative

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3 Ibid., p. 45.
4 Ibid., p. 59.
in entering into a commitment in another Member State, the host country may the life cover subject to its administrative authorization as comparable to the case of mass risks in the non-life insurance.

We should add that harmonization of the national rules is not achieved with respect to the technical reserves as in the Non-Life Insurance Directive concerning the mass risks, and that the principle of cumul does not apply either.

3. The Third Generation

Both the Third Non-Life Insurance Directive and the Third Life Insurance Directive adopt the principle of single licence system or that of home country control. The licence delivered by a home Member State, that is, a Member State where a head office of an insurer is situated, must be recognized by all the other Member States. Thus, an insurer, once licensed by the home country, may carry on business within the entire EC, either through its branches or agencies set up in the other Member States or by way of providing cross-border services.

Such a single licence principle is valid for all the kinds of insurance. The distinction between 'large risks' and 'mass risks' is not maintained any longer nor remains the distinction between the 'own initiative' cases and the others, whereas these distinctions, as I shall mention later, remains significant in terms of the choice of law.

Under the Directives belonging to the first and second generations, each Member State where the insurer carried on business is responsible for regulating the technical reserves. On the other hand, the directives of the third generation empowers the home Member State to ensure that the insurer has sufficient technical reserves to cover its entire business. For this purpose, the Directives lay down harmonization rules for defining and calculating the technical reserves.

It is true that the host Member State does not completely lose the power to control over the activities of an insurer in its territory. However, it must not prevent a policy-holder from concluding a contract with an insurer, as long as that does not conflict with legal provisions protecting its 'general good'.

We should add that the Directives make the home country control more liberal. Prior approval of policy conditions and tariffs by the authorities is not allowed any longer.

B. Private Law

While the Directives primarily deal with prudential control by the supervisory authorities of the Member States, the Directives belonging to the second and the third generations have some rules regulating the private law aspect of insurance. However, they do not seem to attempt to harmonize the national rules on the substantive law level. The cursory inspection allows me to find only few substantive rules laid down in view of the consumer protection, that is, the rule enabling the policy-holder to cancel the life insurance contract within a certain period of time (cooling-off period) and the rule which obliges the insurer to give necessary information to the policy-holder. We may add a substantive rule on the level of private international law from the Third Non-Life Directive: 'Before an insurance contract is concluded, the insurance undertaking shall inform the policy-holder of the law applicable to the contract where the parties do not have a free choice, or the fact that the
parties are free to choose the law applicable and, in the latter case, the law the insurer proposes to choose.


According to Article 1(3) of the Rome Convention on the Law Applicable to Contractual Obligations, the rules of the Convention do not apply to contracts of insurance covering risks situated in the territories of the Member States of the EC. In other words, while the conflicts rules of the Rome Convention apply to the risks situated outside the Community, the rules of the Directives are applicable to those situated within the EC.

According to the same provision, in order to determine whether a risk is situated within the EC, the court shall apply its internal law. This means that the court of each Member State applies its own domestic rules as enunciated in the Directives on this point. It follows that, in the case of life insurance, the risk is regarded as situated in the Member State where the policy-holder has his habitual residence. As far as the non-life insurance is concerned, the Member State where the risk is situated is the Member State where the policy-holder has his habitual residence except the insurance relating to buildings and motor vehicle, and travel insurance.

Article 59 of EEC states that 'restrictions on the free supply of services within the Community shall be progressively abolished.' It may safely be said that the free supply of services can be achieved in its fullest extent by way of the parties being allowed to choose the applicable law. Indeed, in accordance with Article 7 of the Second Non-Life Insurance Directive, as far as the large risks are concerned, the parties may choose any law. The consumer protection is regarded as unnecessary for those risks.

On the other hand, in the case of the mass risks, the applicable law is objectively determined: where a policy-holder has his habitual residence within the territory of the Member State in which the risk is situated, the law applicable to the insurance contract is the law of that Member. However, the party autonomy is not totally excluded for the case of mass risks. It is left to the law to be objectively applied to decide whether the party can choose another law. This rule is based upon the assumption that the protection of policy-holder would be less important if his own law allows the choice of law which might deprive him of the protection.

Article 4 of the Second Life Insurance Directive, in principle, follows the same lines of Article 7 of the Non-Life Directive. It will be sufficient to say that, in the case of life insurance, the place of commitment is adopted as a connecting factor, that is, the place where the policy-holder has his habitual residence.

This way to take into consideration the interests of consumer differs from the way adopted by the Rome Convention in its Article 5. Affirming the principle of party autonomy, the Convention prevents the consumer from being deprived of the protection afforded to him by the mandatory rules of the law of the country in which he has his habitual

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residence. It remains to be seen which way is more preferable to harmonize the necessity of free supply of services with that of the consumer protection.

II. Non-EC Countries and the General Agreement on Trade in Services

A. Non-EC Countries

Once an insurance company whose head office is outside the EC has set up its subsidiary authorized to carry on insurance business within the EC or has acquired an existing EC insurer, the subsidiary will be able to take advantage of the single licence system or the home country control.6

On the other hand, a Member State has no obligation to allow a Non-EC insurer to set up its branch or agency. In addition to the special rules regulating, in particular, technical reserves and solvency margins, a Non-EC insurer must pass the thresholds that an EC-insurer need not cross. For example, a Member State may impose upon non-EC insurers the requirement of contemporary economic conditions: while authorization for branch cannot be refused to EC-insurers on the grounds that the demands of the local market were already satisfied or that further competition is undesirable, the application by non-EC insurers may be examined in the light of the economic demands of the local market.7

A Member State is not obliged to allow a Non-EC insurer to provide cross-frontier services through its branch or agency established within the EC either.

B. General Agreement on Trade in Services

'The Uruguay Round negotiations mark the first attempt to address through multilateral negotiations the elimination or reduction of barriers and distortions in trade in services.' The latest draft of 'General Agreement on Trade in Services' defines trade in services as the supply of a service:

'(a) from the territory of one Member into the territory of any other Member;
(b) in the territory of one Member to the service consumer of any other Member;
(c) through the presence of service supplying entities of one Member in the territory of any other Member. . . .'

These modes of the supply of services appear to coincide with the modes of the services that, under the Third Directives, insurers have the right to supply.

The General Agreement has a clause to the effect that any Member of the Agreement is not prevented from being a party to or entering an agreement liberalizing trade in services between or among the parties to such an agreement (Article V). Naturally, a Member

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7 Ibid., p. 23.
may be a party to an agreement of such economic integration only under certain conditions. Article V of the General Agreement lays down the conditions: such as agreement (a) has substantial sectoral coverage and (b) provides for the absence or elimination of substantially all discrimination, in the sense of Article XVII (national treatment clause), between or among the parties, in the sectors covered under sub-paragraph (a). This paragraph in which the rather vague concept as 'substantially all discrimination' is used is followed by paragraph 2. It reads: 'In evaluating whether the conditions under paragraph 1(b) are met, consideration may be given to the relationship of the agreement to a wider process of economic integration or trade liberalization among the countries concerned.' It would be easily presumed that Japan opposed to this provision designed to allow a concession to certain countries interested in the economic integration.

On the other hand, there is a provision in favour of the third country. Paragraph 6 reads:

'A service supplier of any other Member that is a juridical person constituted under the laws of a party to an agreement referred to in paragraph 1 shall be entitled to treatment granted under such agreement, provided that it engages in substantive business operations in the territory of the parties to such agreement.'

It follows that, when a Japanese insurer set up a subsidiary within a Member State of the EC in accordance with that State's law, it will be able to take advantage of the benefit of this provision. On the other hand, it seems that, when a Japanese insurer set up a branch within the EC, it will not be entitled to that benefit.

III. Reciprocity

Following the Directive of the banking sector of December 15, 1989 (Articles 8 and 9), the Motor Services Directive and the Second Life Insurance Directive now contain the reciprocity clauses. The reciprocity clause laid down in the Motor Services Directive is applicable to all non-life business covered by the First Non-Life Insurance Directive. The relevant provisions are to the same effect in both Directives:

Whenever it appears to the Commission that a third country is not granting Community insurance undertakings effective market access comparable to that granted by the Community to insurance undertakings from that third country, the Commission may submit proposals to the Council for the appropriate mandate for negotiation with a view to obtaining comparable competitive opportunities for Community insurance undertakings (the First Non-Life Insurance Directive, Art. 29B, paragraph 3, the Second Life Insurance Directive, Art. 33, paragraph 3);

Whenever it appears to the Commission that Community insurance undertakings in a third country are not receiving national treatment offering the same competitive opportunities as are available to domestic insurance undertakings and that the conditions of effective market access are not being fulfilled, the Commission may initiate negotiations in order to remedy the situation (the First Non-Life Insurance Directive, Art. 29B, paragraph 4, the Second Life Insurance Directive, Art. 32B, paragraph 4).
The expressions ‘effective market access comparable to that granted by the Community’ and ‘national treatment’ do not seem to be entirely clear. Does it simply mean that the authorization for the establishment should be granted by the third country’s authorities with as much certainty as that granted by the Community? Is the third country required with the reciprocity clause that it should adopt the similar legislation, in other words, it should allow the access to its market as if the third country had no territorial limit?

The other point is whether it suffices that the condition of reciprocity is simply met de jure. According to our Insurance Business Law, before a foreign insurer set up a subsidiary in Japan, prior approval by the competent authority is necessary with respect to, for example, policy conditions and premiums. Is the condition of reciprocity be regarded as satisfied, when such a system is replaced by a more liberal control system? Or does the clause in question go further to require de facto reciprocity? For example, it is said that the Japanese supervisory authorities often would not make any decision for a long time from initial submission of an application for establishment by a foreign undertaking, just saying ‘we are now evaluating your application.’ Does the reciprocity clause mean that the Japanese authorities will not take such an attitude any longer?

The Japanese substantive rules which appear to be relevant to the insurance business in the international sphere are contained in ‘Insurance Business law’ and ‘Law concerning Foreign Insurers.’ The former deals with the case that foreign undertakings set up their subsidiaries in Japan. The latter purports to regulate the business through a branch by a foreign insurer carrying on an insurance business outside Japan. Both were enacted in 1939 and in 1949, respectively, and remain almost unaltered despite the fact that the Japanese market is no longer what it was. Whatever meaning the Commission may give to the ‘reciprocity,’ it will undoubtedly stimulate the movement of the reform of those laws.

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8 For the banking section, see, Vigneron et Smith, Le concept de réciprocité dans la législation communautaire: l'exemple de la deuxième directive bancaire, RMC, pp. 353–354.