

FROM: Director, Worldwide Markets
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SUBJECT: EUROPEAN UNION (EU) ENLARGEMENT

SUBJECT AREA(S): Details of countries acceding to EU membership on 1st May 2004 and implications for the Lloyd's market

ATTACHMENTS: Appendix 1. Outline of the EU insurance régime
Appendix 2. Further information on Lloyd's and the accession countries.

ACTION POINTS: Managing Agents and Underwriters to note

DEADLINE: **Immediate**

1. Background

On 1st May 2004, ten countries will be joining the European Union (EU). These "accession countries" are Cyprus, the Czech Republic, Estonia, Hungary, Malta, Latvia, Lithuania, Poland, the Slovak Republic and Slovenia. By accession day, all pre-existing EU law on insurance is required to have been implemented by the national governments in the accession countries. There are no transition periods which are sometimes used to allow countries time for EU legislation to be implemented into national law.

2. Lloyd's strategy in the accession countries

A review of the trading opportunities for Lloyd's in the eight Central and Eastern European countries (i.e. the ten countries listed above but excluding Malta and Cyprus) was carried out by Worldwide Markets during 2003 and included consultation with individual underwriters and brokers, managing agents and broking firms, and market associations.

Lloyd's is currently seeking a broad range of authorisations in these countries. There are some differences between the expected licensing position in each accession country. Lloyd's is applying for 'establishment' authorisation in Malta and Cyprus but not the other countries, where Lloyd's is seeking 'services' authorisations only and will not be appointing a General Representatives. This licensing strategy is in line with the conclusions of the review carried out by Worldwide Markets, which were subsequently approved by the Lloyd's Franchise Board. Further details can be found in appendix 2 to this bulletin.

The authorisations needed to transact business in are being sought from the Financial Services Authority (FSA) as Lloyd's home state regulator. In some instances, the FSA will need to contact the regulator in the accession country concerned before finalising the application. At present, there is no guarantee that all the necessary authorisations will be in place for underwriters to be able to transact insurance of risks in the accession countries on accession day. See appendix 2 for further details of the arrangements applicable to Malta and Cyprus.

3. Impact on the transaction of business at Lloyd's

Subject to FSA approval, Lloyd's underwriters will

- continue to be able to transact insurance in Malta and Cyprus in very much the same way as currently – on the basis of 'freedom of services' and 'freedom of establishment'.
- be able to transact direct insurance on a 'freedom of services' basis in the remaining accession countries, though underwriters will not initially be able to transact 'freedom of establishment business there.

However

- underwriters will need to comply with relevant conduct of business rules the state where the policy is issued (e.g. on policy content / mandatory clauses)
- There are specific issues relating to the transaction of Motor insurance which will be the subject of a separate market bulletin.

4. Premium Taxes and Parafiscal charges in the accession countries

Legal and tax advice is currently being gathered from each country and this will form part of a further bulletin from Lloyd's Taxation Dept once all information is to hand. On the basis of information so far received, only Slovenia amongst the central and eastern European countries appears to have a 'per transaction' premium tax. It is expected that all taxes and parafiscal charges for the Central and eastern European Countries will be administered via the Lloyd's Central Taxes System, and currently further consideration is being given to how such matters will be treated for Malta and Cyprus. Lloyd's Taxation Department will be issuing a more detailed Market Bulletin on this aspect.

5. New FIL codes

New FIL codes will be introduced for business located in the accession countries which incept on or after 1st May 2004. These codes will be issued to the market once legal advice on business conduct rules in each accession country is to hand.

6. Further information

Additional information on the general principles of the EU insurance régime can be found at appendix 1 and fuller detail on the opportunities for underwriters in each of the accession member states can be found at appendix 2, both attached to this bulletin.

The *Lloyd's in Europe* "glancecard" summarising details of what underwriters can do in Europe, and providing details of Lloyd's European representation, does not currently include

information on the accession countries, except Malta and Cyprus. This will be updated and reissued once formal confirmation of Lloyd's authorisations has been received from the FSA.

Underwriters and brokers interested in seeing the Worldwide Markets publication "Opportunities in Central Europe" may do so via the Lloyds.com website at the following address <http://www.lloyds.com/index.asp?ItemId=4168> . This information is password-protected and password information for those who have not already been allocated passwords can be gained from

Market Services at box 190 in the Underwriting Room, or by telephoning 020 7327 6677 (e-mail Market.services@lloyds.com)

Further information about the content of this Bulletin may also be obtained from Lloyd's Worldwide Markets as follows

Alex Faris, 020 7327 6854 (e-mail: Alexandra.c.faris@lloyds.com) regarding the regulatory framework in the accession countries in Central and Eastern Europe

Marianna Papadakis, 020 7327 6802 (e-mail Marianna.papadakis@lloyds.com) and/or Zoë Kilminster, 020 7327 5772 (e-mail Zoe.kilminster@lloyds.com) for queries relating to Malta and Cyprus

Simon Wilson, 020 7327 6637 (e-mail: simon.wilson@lloyds.com) for information regarding the publication "Opportunities in Central Europe".

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Appendix 1. General Outline of the EU Insurance régime

The EU insurance régime comprises many directives dating back to the early 1970s. In essence, an insurer is financially supervised by the regulatory authorities in the country of its head office (“home state” supervision), and subject to authorisation by this supervisor, may trade throughout all EU member states. This principle of the ‘single licence’ is fundamental to the EU insurance régime and any authorisation by an insurer’s home state supervisor is given on the basis of mutual recognition across all member states.

Insurance underwritten by an EU insurer may be transacted on either a ‘freedom of establishment’ or ‘freedom of services’ basis.

The overwhelming majority of EU (but non-UK) business written at Lloyd’s occurs on a *Freedom of Services* basis, with no underwriting decision being taken locally: rather, the decision is taken by the underwriter in London. So, for example, open market business would be considered as Freedom of Services as would business transacted under a binding authority where the coverholder’s activity is limited to the issuing of insurance documentation.

Freedom of Establishment business occurs where the decision to accept risk is made in the country concerned: typically, business involving underwriting decisions being taken under delegated authority by a coverholder outside the UK qualifies as ‘establishment’ business in the country of risk.

Whilst the financial supervision of insurers is carried out on a home state basis, there are certain aspects of insurance supervision which remain subject to ‘host state’ supervision, within the EU framework. These principally include marketing and selling, and contract law in respect of ‘mass’ (i.e. principally personal lines) risks. Premium taxes and parafiscal charges are also subject to the rules of the country where the risk is located.

Appendix 2. Further details on Lloyd's trading position in each 'accession country'.

The EU insurance directives set out that there are 18 separate classifications of non-life insurance. An insurer must be specifically authorised by its supervisor to transact business in each desired classification. Lloyd's is currently in dialogue with the Financial Services Authority (FSA) with a view to seeking a broad a range of authorisations in the accession countries. However, Lloyd's will be applying obtain 'establishment' and 'services' authorisations in Malta and Cyprus, and 'services only' authorisations in the other accession countries.

Lloyd's is also taking legal and tax advice on the implications of writing business in each accession country and further information will be issued once this advice is to hand. When received, this advice could in theory affect the classes of business for which formal regulatory authorisation will be sought.

Malta and Cyprus

Lloyd's is already a licensed insurer in Malta and Cyprus with representation currently in place and coverholders already operating in both countries. In EU terminology, the current position is equivalent to authorisation on both a 'services' and 'establishment' basis. Subject to approval by the FSA in consultation with the national Regulator in each country, it is hoped that Lloyd's will continue to be able to trade the same classes of insurance as currently (i.e. either on an 'establishment' or 'services' basis – or both), after accession.

Lloyd's Worldwide Markets will be continuing bi-lateral discussions with the Maltese and Cypriot regulators with a view to securing agreement to allow the pre-existing trading arrangements in these countries to continue if necessary after accession day until the new authorisations are confirmed by the FSA.

Central and Eastern European Accession countries

A review of the trading opportunities for Lloyd's in these countries was carried out by Worldwide Markets during 2003 with consultation from individual underwriters and brokers, and market associations. Lloyd's is currently neither a licensed insurer in these countries, nor do we have local formal representation there.

As stated in the covering bulletin, Lloyd's will be seeking a broad range of 'services' licenses in these countries but is not applying for an 'establishment' authorisation in these countries and will not be appointing a General Representative in each one. This licensing strategy is in line with the conclusions of the Worldwide Markets review, which were approved by the Lloyd's Franchise Board.

Furthermore, in view of the complexities and additional reporting requirements involved with the transaction of compulsory third party motor vehicle liability business, it has also been decided NOT to seek formal authorisation to underwrite such motor business in these eight countries.

Therefore, syndicates will NOT initially be permitted to transact

- Coverholder business in respect of any class of business, for coverholders located in these eight countries; and
- Compulsory third party motor vehicle liability insurance business for vehicles registered in the eight countries

However, this situation will be kept under review and any Managing Agent wishing to extend the territorial scope of business for Lloyd's coverholders who are already approved may, subject to the rules of the normal coverholder approval process, apply to the Lloyd's Coverholders Department to have their territorial approval extended to one or all of these eight countries on a 'services' basis. In addition, any Managing Agent wishing to write motor insurance for vehicles registered in these countries will need in the first instance to contact Lloyd's Worldwide Markets.