COMMISSION DECISION

of 4 December 1992

relating to a proceeding pursuant to Articles 85 of the EEC Treaty

IV/32.797 and 32.798 — Lloyd's Underwriters' Association and The Institute of London Underwriters

(Only the English text is authentic)

(93/3/EEC)

THE COMMISSION OF THE EUROPEAN COMMUNITIES,

Having regard to the Treaty establishing the European Economic Community,

Having regard to Council Regulation No 17 of 6 February 1962, First Regulation implementing Articles 85 and 86 of the Treaty (1), as last amended by the Act of Accession of Spain and Portugal, and in particular Article 2 thereof,

Having regard to the notification and application for exemption and/or negative clearance of 7 June 1989 submitted to the Commission by Lloyd's Underwriters' Association and the Institute of London Underwriters of two agreements, namely the Joint Hull Understandings (JHU) and the Respect of Lead Agreement (RLA),

Having regard to the Commission Decision of 1 October 1990 to initiate proceedings in this case,

Having regard to the summary of the application and notification published (2) pursuant to Article 19 (3) of Regulation No 17,

After consulting the Advisory Committee on Restrictive Practices and Dominant Positions,

HAS DECIDED AS FOLLOWS:

I. THE FACTS

A. The notification

(1) On 7 June 1989 the Institute of London Underwriters (ILU) and Lloyd's Underwriters' Association (LUA) formally notified to the Commission for negative clearance or exemption two Agreements referred to as the Joint Hull Understandings (JHU) and the Respect of Lead Agreement (RLA). This formal notification was preceded by an informal notification and submission in relation to both Agreements by letters dated 7 July 1988. The notified Agreements relate to marine hull and machinery insurance.

B. The associations of undertakings

(2) The ILU is an association of insurers (underwriters) offering marine and aviation insurance in London. Founded in 1884, it provides the usual functions of a trade association including various administrative support services for members. It has approximately 112 members of which 50 % are British-owned companies. The other half comprises subsidiaries or branches of companies from around the developed world.

(3) Lloyd's of London is an incorporated society of private underwriters who provide an international market for almost any type of insurance. It has a premium income of approximately £ 6 000 million per year. Three-quarters of this business comes from outside the United Kingdom. Policies are subscribed by private individuals whose liability is unlimited. There are currently some 31 000 members who are grouped into some 400 syndicates. A specialist underwriter agent accepts business on behalf of each syndicate. Members may join more than one syndicate.

(4) LUA was founded in 1909 and represents all Lloyd's syndicates which handle marine business, of which there are approximately 230.

(5) The two Associations operate a number of joint committees whose purpose is to monitor topics of interest in particular fields and which brings together specialists in each field. One of these committees is the Joint Hull Committee (JHC) referred to below. The JHC comprises 16 people drawn in equal numbers from the LUA and ILU. The JHC's *raison d'être* is to consider matters of market interest and to develop and administer the two notified Agreements — the JHU and RLA.

(6) ILU and LUA represent the vast majority of underwriters active in marine insurance in London. Together, they account for approximately 90 % of the United Kingdom's total marine insurance capacity, the remainder being provided by a few companies outside the two Associations.

(1) OJ No 13, 21. 2. 1962, p. 204/62.
(2) OJ No C 87, 8. 4. 1992, p. 4.

C. The Market

(7) Marine hull insurance is written mainly in the USA, France, Norway and the United Kingdom. The United Kingdom share of international hull business is a significant part of the world total for hull insurance not subject to compulsory localization requirements. The parties estimate that approximately 25 % of Community hull business is insured in London and that a higher proportion of vessels from outside the EEC is insured in London. The parties have also said that the London market's reputation in the marine insurance business means that many risks are 'led' (i.e. initially but partially placed) in London with other foreign markets following the London market's judgment on rating and claims settlements so that to some extent the 'London market's influence is somewhat greater than its true market share'.

(8) Total premiums earned by the two Associations from marine insurance is estimated to be approximately £ 4 000 million per year of which £ 3 000 million is hull and machinery insurance.

(9) Shipowners generally use insurance brokers to handle business on their own behalf to ensure that their fleets are placed on the best possible terms to be found in any markets anywhere in the world. According to the applicants 'competition on hull business tends to be between rather than within markets'. Thus, the London market as a unit competes directly with other markets with risks being switched between markets where brokers obtain better terms from a different market but there is little competition within the London market itself which is initiated by underwriters. The market relies upon brokers to initiate competitive requests.

(10) Marine insurance is characterized by the fact that it is normally done on a co-insurance basis, i.e., because of the large amounts of money involved, underwriters almost always seek to share exposure on a given risk by limiting participation to an agreed proportion of the whole. Sometimes a particular risk is placed in more than one market (i.e. in both London and, for example, France). It is usual, even for co-insurers, to seek reinsurance for part of the risk and, where the risk is covered partly in another market, the underwriters in that other market may reinsure in London.

(11) Another characteristic of this market is that only a few underwriters (known as leaders) consider any particular risk in detail, evaluating the risk and assessing appropriate conditions and premiums. The remainder (known as followers) rely largely on the judgment of the leaders to decide whether they too should participate so that the reputation of the leader is of some importance in helping the broker obtain following support in the market. The placing of a risk is done by means of a 'slip' or order form which gives details of the risk and the cover proposed. A typical placing of a marine hull risk would involve some 20 underwriters and could be as large as 50 where the sums involved are very large.

(12) Similarly when claims are made, although each underwriter theoretically has the right to decide for himself, in practice the leaders make the decision and followers merely review it briefly. Payments are made centrally as are premiums.

(13) A further distinguishing feature of hull insurance is that it has a 'long tail', i.e. a long time may elapse between payment of premium on the one hand and the reporting and payment of claims on the other. Most claims are made well after the policy year in which the damage occurred, usually in the third or fourth year and very few, other than major casualties, are even reported before the second year. This is why at renewal the insurer does not take into account solely the current year's results but rather several years and, if possible, as many as eight years. This period is thought to be adequate to give a complete pattern of losses and claims and to give an indication of when losses occur and when claims are made.

(14) According to the applicants, 'the main focus for competition is on price, with claims settlement experience and the security and reputation of the insurance carriers also carrying considerable weight'.

(15) Other characteristics of this market are the high frequency of claims and the role of the owner, crew and other variables in assessing the risk. The importance of these additional factors, and particularly that of the owner, mean that 'in hull insurance one vesseld could be insured at more than ten times the premium payable for an identical one owned by a shipowner with a good record.'

D. The Agreements as notified

(i) *The Joint Hull Understandings (JHU)*

(16) The JHU contained three clauses (clauses 3, 2B and 11) which limited the freedom of the members of ILU and LUA to determine their own prices, particularly on renewal. These clauses, following the issuing of a statement of objections, ceased to be applied by LUA and ILU on 25 April 1991. These clauses are described below.

(17) Clause 3 referred to a 'Graph' annexed to the JHU. This graph set out recommended minimum premium increases for a given loss ratio. The rate of increase increased as the loss ratio worsened. For example, for a single vessel with a 17 % credit balance or loss ratio (i.e. premiums paid exceed losses by 17 %) the increase was 53 %. If the balance went into debit at say — 25 %, the rate of increase would be 90 %. For larger fleets, the rates could vary within a certain band and the rates within the bands were lower than those applying to single vessels. For ratios (i.e. debit balances) in excess of — 25 %, the leaders were free to charge such further increases as they thought appropriate. If the terms of renewal were below the minima set in 'the graph, it is strongly recommended that the four leaders should consult before any quotation is made and the result of their deliberations reported to the Joint Hull Committee'. This freedom to depart from the graph was introduced on 9 February 1989. Prior to that date, underwriters were not free to depart from the graph unless the consent of the JHC was obtained. No sanctions existed where underwriters chose to depart from the graph unilaterally other than, according to the applicants, 'strong criticism ... of the leading underwriters concerned or if the case was serious enough, the chairman of the Joint Hull Committee or his deputy may speak privately to the underwriter or underwriters regarded as having been at fault'.

(18) Since the graph had been in existence for 'longer than any serving underwriter can remember' the parties were not able to explain how exactly it was first drawn up. The parties have, however, explained that it reflected 'general market experience' and that changes to it were made after a general assessment of such factors as 'exchange fluctuations ..., inflations, and changes in shipbuilding and repair costs'.

(19) Clause 2B provided that where results call for an increase then the 'excess' (referred to as the 'deductible') should be increased by 50 % 'of the percentage rise ... with a minimum increase of 10 %'.

(20) Clause 11 stipulated that where payment was not made in cash immediately but was deferred, the rebate which is normally available for prompt cash payment was to be reduced from 15 % to 10 %.

(21) Clause 1 (a) of the notified JHU provided that 'Hull quota share and obligatory surplus reinsurance contracts shall be restricted to flag and ownership/management FOM business of the country concerned unless specifically agreed by all underwriters'. This meant that, unless otherwise specifically agreed, reinsured business was restricted to vessels whose country of registration, ownership and management was the same as that of the reinsured. This clause was amended at the request of the Commission and now contains a recommendation that reinsurers should ask for information on the nationality of the vessels' owners as this is considered to be a material fact affecting the assessment of risk.

(22) The remaining clauses of the JHU provide guidelines and uniform criteria on the technical detail of policy renewals. Essentially, they identify prudent market practices and provide methods for reducing confusion over the true record of the insured or of the scope of the hull and machinery policy. Underwriters are free to ignore these guidelines and use others should they so wish. They relate to such questions as :

(a) the methodology for classifying vessels ;

(b) the need for information about the shipowner and his record to be presented in a uniform manner (so as to facilitate comparisons and prevent misrepresentation) ;

(c) the treatment of changes in value of vessels and in particular the need to differentiate between increases which are merely designed to keep pace with inflation and those which increase the vessel's propensity to partial loss ;

(d) the valuation of vessels for partial and total losses and in particular the need to ensure that the valuation of vessels for partial and total loss does not diverge unduly ;

(e) the centralization and administration of refunds for periods when vessels are in port — when a vessel is in port it is subject to a lower risk than if it were fully operational. In recognition of this, a refund is normally made to the assured. The amount of and reference period for the rebate is freely negotiated at the time of conclusion of each insurance contract. The claim for refund is made to a central office, run by LUA/ILU, whose staff has expert knowledge of ports and port conditions around the world and which verifies that the vessel has actually moored for the period claimed. The clause refers to refunds for completed periods of 30 days which is the normal reference period. However, every underwriter or group of underwriters is free to give refunds for periods of less than 30 days;

(f) the need not to forfeit or prejudice the insurers' legal right to question the 'seaworthiness admitted' clause;

(g) the need for mortgagees to obtain separate cover since the hull and machinery policy does not indemnify them against the improper conduct of the owner;

(h) the definition of the risks covered by the hull and machinery policy.

(ii) *Respect of lead agreement (RLA)*

(23) This agreement provided essentially that the same leaders who first underwrote hull business should be allowed to continue as leaders when the policy came up for renewal. Following underwriters or other potential leaders were prohibited from attempting to 'lead' on the renewal. This meant that other underwriters were deprived of the opportunity of bidding or competing for renewal business and that shipowners were deprived of the choice and possibly cheaper prices which competition between competing leaders would afford.

(24) Furthermore, pursuant to clause 1 of the RLA, the members of the two Associations agreed not to subscribe to any slip unless two leaders from each Association were signatories (except where a non-signatory was a leader prior to the signing of the RLA). This meant that competition between the ILU and LUA was prohibited in principle.

(25) The RLA was adhered to by almost all members of the ILU and LUA. If the member breached the agreement, his Association (either ILU or LUA) could announce that he was deemed no longer to adhere to the agreement. The effect of this announcement was that no other underwriter could follow his lead. This occurred on at least one occasion and although the parties claim that the underwriter concerned 'lost no business as a result', the announcement was still felt to be 'a worthwhile sanction'.

(26) The LUA and ILU, at the request of the Commission, abandoned this agreement on 25 April 1991. It has been replaced by a new text (the 'new RLA') which provides:

1. Where a risk for renewal is being quoted by a competing group or groups of underwriters the leader(s) of the competing group(s) may consult the existing slip leader(s). If consulted, the existing slip leader(s) will make available their records of the fleet statistics.

2. The existing slip and competing slip must not discuss their proposed renewal terms.

3. Underwriters currently suscribing to the existing slip must give the leader of their slip notice, at the latest two months prior to the renewal date of the first vessel, of their intention of leaving the existing slip to join a potentially competing slip.

   The notice provision does not apply if the competing slip is covered as to 100 %.

E. Observations from third parties

(27) The Commission has received no observations from interested third parties following publication of the notice required by Article 19 (3) of Regulation No 17.

II. LEGAL ASSESSMENT

ARTICLE 85 (1)

A. Decisions of associations of undertakings

(28) The ILU and LUA are associations of undertakings within the meaning of Article 85 (1). The JHU and the RLA each constitute decisions of associations of undertakings within the meaning of Article 85 (1).

B. Effect on trade

(29) An agreement relating to marine insurance which involves transport is one which, by its very nature, is liable to affect trade between Member States. In addition, trade is affected because the ILU and LUA members provide this service to shipowners or through brokers who are established in other Member States. Furthermore, given the United Kingdom market share of the members of the two Associations (almost 100 %) this effect can be said to be appreciable.

C. Restrictions of competition

(i) *The Joint Hull Understanding (JHU)*

The JHU contained three clauses which restricted competition contrary to Article 85 (1):

(a) Clause 3 — The graph

(30) The graph was equivalent to a price fixing agreement. Its object was to prevent renewals being agreed at rates which were below the minima indicated in the graph. It limited the scope for leaders to negotiate different rates at renewal from those indicated in the graph. Until 9 February 1989, the members of the two Associations were obliged to respect the rates indicated in the graph. If they did not, although there were no sanctions, such underwriters were generally 'criticized' by their fellow underwriters. The absence of sanctions did not, however, mean that there was no price fixing agreement within the meaning of Article 85 (1) since such an agreement by its very nature restricts competition and is explicitly prohibited by Article 85 (1).

(31) In so far as the effect is concerned, the applicants could not determine exactly the number of times the graph may have been breached. They did, however, state that to their own knowledge 'a number of renewals' each year would have been in breach of the graph. In other words, the vast majority of renewals complied with the minima set in the graph, while breaches of it were regarded as somewhat exceptional.

(32) Furthermore, the fact that from 9 February 1989 until 25 April 1991 the parties were free to depart from the graph does not mean that there was during this period no infringement of Article 85 (1).

Recommended price increases also fall within the prohibition in Article 85 (1) [1]. The fact that there continued to be an obligation to report deviations from the graph would also have acted as a dissuasive factor and would have tended therefore to re-enforce the restrictive nature of the graph.

(b) Clause 2B

(33) The clause limited the freedom of underwriters to set their own levels for increases in deductibles (excess) and was therefore restrictive of competition within the meaning of Article 85 (1).

(c) Clause 11

(34) It is established law [2] that an agreement as to the amount of rebate to be granted is caught by the prohibition against price-fixing in Article 85 (1). Clearly the clause implied that there was an underlying agreement that a rebate of 15 % should be available for immediate payment in cash. Where payment is deferred, this rebate is required to be reduced to 10 %.

(35) The abovementioned clauses were deleted by the ILU and LUA on 25 April 1991.

(36) The remaining clauses of the JHU are of a technical nature and do not contain any provisions which appreciably prevent, restrict or distort competition within the common market.

(ii) *The respect of lead agreement (RLA)*

(37) The RLA restricted competition in the London market by effectively ensuring that the same leaders who first insured the risk continued to underwrite that risk at renewal. These leaders were thus protected from competition from potential competing leaders who might have wished to offer better terms or prices. This agreement was abandoned by the ILU and LUA on 25 April 1991 and replaced by a new agreement.

(38) The RLA also restricted competition between the ILU/LUA by providing that there should be two leaders from each Association on every 'slip' (order). Brokers were therefore not free to concentrate their attention on one Association where they so chose or where this might have produced cost savings and better prices.

[1] German fire insurance case: Commission Decision 85/75/EEC, OJ No L 35, 7. 2. 1985, p. 20, and Case 45/85 Verband der Sachversicherer v. Commission [1987] ECR 405.

[2] Joined Cases 209 to 215 and 218/78 Van Landewijck v. Commission [1980] ECR 3125; Joined Cases 240 to 242, 261, 262, 268 and 269/84 Stichting Sigarettenindustrie v. Commission [1985] ECR 3831.

(39) The new RLA permits a competing group or groups of underwriters to challenge the existing group (or 'slip'), obliges the latter to make available their records of fleet statistics so as to facilitate the competing group's task of assessing the risk and prohibits any discussion of renewal terms between the existing and competing group of underwriters. For these reasons it can be concluded that the new RLA does not contain any clauses which appreciably restrict, prevent or distort competition within the common market,

HAS ADOPTED THIS DECISION:

Article 1

On the basis of the information in its possession the Commission has no grounds for action under Article 85 (1) of the EEC Treaty in respect of the notified agreements as modified, namely the new joint hull understandings and respect of lead agreement.

Article 2

This decision is addressed to the following associations of undertakings:

— Lloyd's Underwriters' Association,
Lloyd's,
1 Lime Street,
UK-London EC3M 7HA,

— The Institute of London Underwriters,
49 Leadenhall Street,
UK-London EC3A 2BE.

Done at Brussels, 4 December 1992.

For the Commission
Leon BRITTAN
Vice-President