Implications of the European Commission guidance on Test-Achats ruling
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Implications of the European Commission guidance on Test-Achats ruling

On 22 December 2011 the European Commission (EC) issued a guideline on the application of the now widely known European Court of Justice (ECJ) Test-Achats decision on gender specific insurance tariffs. The following article will have a closer look at some of the important questions of the decision and the guidance recently issued by the EC.

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Current situation

Neither the ruling (see box for details) nor the guideline themselves supersede local regulations in the member states automatically. Indirectly the court decision has given local legislators a deadline by referring to the review date 21 December 2012 as an absolute end-date to current practice. Thus it is necessary that local legislators take actions by then in order to make an amendment to the applicable law/ regulation within the requirements set forth by the court and the EC guidance.

It is still hard to predict what approach local legislators will take to implement the court decision as it stands. At first the decision left considerable room for interpretation which could have led to differing implementations in the different member states. However, the EC’s guideline clearly sets out the scope and limits of the court decision. It also expresses the EC’s intent to hamper any diverging interpretations amongst the different member states that could have a negative effect on the implementation of the unisex rule.

Geographical scope

The court decision applies to all insurance policies sold from EU insurers to individuals who live in the EU. At the same time, EU insurers can offer insurance policies outside the European Union using gender as a rating factor unless local legislation states differently.

As a general rule, the prohibition of using gender as a rating factor also applies to Non-EU insurers when offering and marketing insurance policies in the EU. Under limited circumstances it might still be possible to sell insurance policies to individuals using gender as a rating factor. For example, in some countries it is recognised that insurance policies concluded by way of correspondence (letter, telephone, internet or other means of communication) are free from supervision or are only under limited supervision (e.g. correspondence insurance in Germany). Thus, an insurance policy offered in Switzerland and bought from an individual that lives in the EU could still use gender as a rating factor. However, as soon as any intermediary (middleman) acts for the insurer or as soon as this insurer does any other marketing in the EU, the general rule would apply, restricting such a practice.

New contracts

The question that arose immediately after the publication of the court decision was whether the judgment is applicable only for business entered into after 21 December 2012. The

“Association Belge des Consommateurs Test-Achats ASBL and others” or better known as simply “Test-Achats” is the name of the ECJ ruling that caught the European Union (EU) insurance industry by surprise on 1 March 2011. The Belgian consumer group had successfully challenged Article 5 (2) of the council directive 2004/113/EC (Gender Directive) arguing that it stands in conflict to the overall EU principle of equal treatment of men and women (Case C-236/09).

In its reasoning the court agreed with the argumentation of the consumer group and concluded that the current derogation in Article 5 (2) of the council directive 2004/113/EC (Gender Directive) which allows insurance premium or benefits to differ by gender if based on relevant statistical data in pricing risk is contrary to the fundamental principle of equal treatment between the sexes as enshrined in the Treaty on European Union.

The ECJ pointed out that the ultimate legislative goal has to be equal treatment. The court reasoned further that such ultimate goal is not reflected in Article 5 (2) of the Gender Directive since it does not foresee any obligation for state legislators to move from a transition period that allows insurance premium or benefits to differ by gender under certain circumstances into an obligatory unisex risk assessment.

As a consequence the court ruled that Article 5 (2) of the Gender Directive is invalid with effect from 21 December 2012. Recognising the current widespread use of such a rating factor within the insurance industry, the ECJ has imposed this transitional period ending on 21 December 2012 for the Governments of member states to abolish the derogation in national law by which time it will become unlawful discrimination to have individuals’ premiums or benefits differ by gender.
court decision did not expressly deliver an opinion on the subject and therefore, the EC took the opportunity to clarify this point in the guidance. According to Art 5 (1) of the Gender Directive, the unisex rule will only apply to “new contracts”. As the term “new contracts” is neither defined in the Gender Directive nor in any national laws of member states, the EC clearly views this as an autonomous concept of EU law which must be interpreted uniformly throughout the EU; any diverging approaches within the various member states would endanger the comprehensive application of the unisex rule which would not be in line with the objective of the Gender Directive – and the judgment in Test-Achats – to ensure the equal treatment of women and men in the EU.

Thereafter, “new contracts” in terms of Article 5 (1) of the Gender Directive are such contracts where a contractual agreement requiring the expression of consent by all parties is made, including an amendment to an existing contract and the latest expression of consent by a party that is necessary for the conclusion of that agreement occurs as from 21 December 2012. Consequently, not only contracts concluded for the first time on or after 21 December 2012, but also any acts on or after 21 December 2012 with the effect to extend contracts that otherwise would have expired, have to be considered as “new contracts”. However automatic extensions of a pre-existing contract, adjustments made to individual elements of an existing contract, taking out of a top-up, and the transfer of an insurance portfolio from one insurer to another shall not fall under the Article 5 (1) Gender Directive. For existing contracts the possibility of making adjustments to individual elements seems to be very interesting for insurers and might incline insurers to adapt existing policies before 21 December 2012 if this has not already happened or has not been foreseen at the inception date of the policy. As an example to mention here is reviewable life business in the UK where the policyholder’s premium can be reviewed every 5 years and adjusted according to an agreed pattern without the consent of the policyholder; such an adjustment would in our view not constitute a “new contract” in terms of Article 5 (1) Gender Directive if it is foreseen in the policy.

2 • European Commission Guideline paragraph 9
3 • European Commission Guideline paragraph 11
4 • European Commission Guideline paragraph 12 (b)
5 • European Commission Guideline paragraph 13 (a)
Group insurance business

The original Gender Directive is concerned with discrimination of individuals in access to and supply of services, explicitly naming as a scope all those offering goods and services to the public. Group insurance is not a service offered to the public directly, and therefore, strictly speaking, not in the scope of the directive. In addition, one could argue that only the people within the respective group at hand are in a comparable situation in the first place, so discrimination between men and women could only be judged adequately within that group itself. As a consequence, as long as the individuals within that group do not pay gender differentiated premiums, e.g. because their employers pay all premium, gender differentiated group insurance pricing should not constitute discrimination.

Pension funds or pension insurers

Governed by a different directive than insurance, being employer related, the so-called Equal Opportunities Directive 2006/54/EC (see table of Anti-Discrimination Directives for details), the Gender Directive and therefore the ruling are not applicable to occupational pension schemes in general.

However, the distinction to be made is whether the contracting party is the employer or the employee directly without involvement of the employer. The Gender Directive is applicable in the latter case. According to the guidelines of the European Commission, the Equal Opportunities Directive and especially Article 9 (1) (h) of this directive, which enables setting different levels of benefits between men and women when justified by actuarial calculation factors, should not be affected by the Test-Achats ruling: not only is its scope of occupational pensions clearly separated, but also is the phrasing of Article 9 (1) (h) of the Equal Opportunities Directive different to that of Article 5 (2) of the Gender Directive.

### Anti-Discrimination Directives and respective proposals

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Reinsurance

Following the judgment and the Commission’s guideline it is clear that reinsurers will not be obliged to price on a unisex basis as long as this does not lead to gender differentiation at the individual level. The Gender Directive is concerned with discrimination of individuals in access to and supply of services, explicitly naming as a scope all those offering goods and services to the public. Reinsurers do not provide services to the public, rather to insurance companies only.

However, we believe unisex pricing could become more important in some reinsurance markets, where insurers want to align the reinsurance conditions with their original terms. It should be noted, though, that due to higher sums assured by male policyholders, the gender split in e.g. a standard surplus reinsurance contract in general would be different than in the underlying portfolio. Therefore, a simple literal transition of the existing reinsurance structure to one priced on a unisex basis would actually add an additional source of uncertainty about net profitability of the portfolio. The insurer might instead consider applying any of the steering mechanisms for the gender mix mentioned below, or take out specific reinsurance which would reimburse for higher claims load due to significantly adverse gender mix.

Reserving

There is no stipulation from the judgment as to whether reserves should be on a unisex or gender differentiated basis. This has been affirmed by the European Commission’s guideline. There will still be the possibility to ask for the gender of the individual and so policy reserves can still be calculated and be gender specific. When pricing on gender neutral terms the individual gender specific reserves would be significantly different for each sex given the premiums charged will either be too little or too great. At an aggregate level these should cancel out except to the extent that negative reserves are unable to be held, for example under French GAAP, in which case

Differences in sums assured between men and women lead to differing gender mix in reinsurance

![Graph showing differences in sums assured between men and women lead to differing gender mix in reinsurance](image)

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6 European Commission Guideline paragraph 14
7 European Commission Guideline paragraph 14
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the reserves at a portfolio level would increase. This situation might change under Solvency II.

For some markets, gender neutral reserving will become market practice. In Germany, for example, there is one product – "Riester-Rente" – being sold unisex already by regulation, which is also reserved unisex basis already for practical reasons: for one to remain in line with pricing basis, and moreover, since surrender values are currently linked to the reserves – and therefore do constitute a benefit which needs to be aligned. All the while, insurers are obliged to prove sufficiency of reserves via proof of adequacy of their assumptions on the gender split.

Medical underwriting

There has been significant uncertainty as to how the Test-Achats ruling would affect medical underwriting and whether a company would still be able to apply the underwriting terms from the implementation date. While there have been various industry meetings since the court decision, these have mainly highlighted the uncertainty rather than alleviating it; the industry did agree however on the main areas of potential impact, these being:

• Collection of information.
• Family history.
• Diseases that have a different effect according to gender.
• Tests which have different result assays.
• Factors which affect gender differently.

Although the overarching principle of the ruling is that benefits and premiums cannot be different simply due to gender, the recent EC guidance has recognised the fact that insurers need to take specific risk factors into account and have stated that these practices are not affected by the ruling and therefore can continue, subject to national legislation. This means that insurers are still able to reflect physiological differences between genders in the questions they ask on the application form, the tests that are requested and the way in which the results are interpreted. It is encouraging that the guidance has provided additional clarity and also addressed the areas of concern to provide clear guidance. Some of the examples cited in the guidance as practices that are allowed to continue are as follows:

• The application form can still be used to collect information on gender and specific gender diseases, e.g. requesting information for a female with a family history of breast cancer.
• The matter of whether ratings can be applied for an adverse family history of breast cancer to only female applicants has been addressed and supported by the ruling.
• Some conditions or risk factors may impact both genders but with a different severity; these can continue to be assessed on a gender specific basis, e.g. hemochromatosis.
• When interpreting test results and different reference values, it is possible to take account of the different reference ranges for men and women and apply the necessary ratings accordingly, e.g. haemoglobin levels.
• The knowledge that men and women process alcohol differently due to their physical differences, can still be taken into account and therefore a different approach can apply to each gender.

As the guidance has clarified, our industry can continue to apply the necessary underwriting terms and as such insurers and reassurers will not have to make amendments to their underwriting manuals or philosophies.

Other risk factors

The guideline implies that it does not expect any implications on other risk factors, even in the light of the currently discussed General Anti-Discrimination Directive.

Product design

In some markets the ruling will lead to an increase of alternative differentiation criteria. Particular innovation in terms of plain workarounds (e.g. rating by shoe size) poses in our opinion a high legal and reputational risk to be accused of equally prohibited “indirect discrimination” (see box for definitions). Neither will insurers be able to simply split their products into separate male and female products with different premiums or benefits. In our view it should be possible however to sell products that by design and through their specific terms and conditions appeal in particular to the one gender, while not per se excluding the other. However a lot of care would have to be invested, though, as products that merely discourage one gender through vital exclusions (e.g. exclusion of breast

8 • European Commission Guideline paragraph 14
9 • European Commission Guideline paragraph 20
cancer which is typically for women or prostate cancer which is typically for men) could run high risk of being interpreted as indirect discrimination.

### Definition of direct and indirect Discrimination

**Direct discrimination** occurs where one person is treated less favourably than another is, has been or would be treated in a comparable situation, on any of the protected grounds.

**Indirect discrimination** occurs where an apparently neutral provision, criterion or practice would put persons at a particular disadvantage compared with other persons on any of the protected grounds, unless that provision, criterion or practice is objectively justified by a legitimate aim and the means of achieving that aim are appropriate and necessary.

### Marketing and distribution

Article 5 of the Gender Directive only covers the calculation of premium and benefits. As such it should be possible for insurers to design and market their products to a specific clientele, as long as they do not discourage or exclude one gender from buying.\(^{11}\) Such exclusion would clearly not be allowed by the European Gender Directive since it is not justified by a legitimate goal.

### Pricing

From 21 December 2012 calculating a unisex rate will of course depend on the expected future mix of male and female lives. The expectation of this will of course depend on the past business mix. However, consideration will need to be made as to the extent that policies are effectively re-broked as female life policies for example may no longer be moved once the unisex rates are brought in as it would be more expensive to do so. Therefore the mix between the sexes will change pushing the mix towards the male lives thereby exacerbating this issue further as the unisex rates increases upwards. Similarly for business covers where the proportion of male lives at higher sums assured are likely to be higher thus offsetting and potentially reversing any normal sum assured discounts. The individuals may instead take out several smaller sum assured policies as this may work out cheaper.

However, insurers should potentially already be considering their pricing bases for current new business rates rather than waiting until the 21 December 2012. The reason for this is that where level premiums are charged which are dependent upon the future assumed persistency of the policies the lapse patterns over the next couple of years are likely to change once unisex rates come into the market. For example, for life insurance policies sold to female lives then from December of this year it will be more expensive for these lives to take out a new policy and so they are potentially more likely to keep their existing policy and not lapse and re-enter. If the insurance rates are lapse supported then a loss could occur on the existing business as these lapse profits won’t come through. The converse is true for male lives where potentially there could be a greater level of lapsing as it could be cheaper for them to move to a new policy than sustain an existing one. However, a loss could again occur should the policies that lapse be only the healthy lives, i.e. the lapsing is anti-selective, leaving more of those policies that are likely to claim. Consideration of these effects should be allowed for when pricing business at the current time.

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\(^{10}\) European Commission Guideline paragraph 15
\(^{11}\) European Commission Guideline paragraph 14
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Conclusion

Both regulations in force and those insinuated by the guideline allow a clear way forward for life insurance business models. Therefore insurers should now look to secure these legally in their territory.

However, no law can prevent respective appeals to court with regard to discrimination just as the Test-Achats case, where results are always uncertain. Public interest in the private life insurance industry, being naturally profit oriented, is currently obviously hard to promote. Let alone the abstract concepts of risk adequate pricing it deems so vital. So when cases like these really come to court (or to the press) one cannot always expect the public or judges will see things like the insurers.

Therefore it should be in the own interest of the insurance industry to actively remove access barriers to their services wherever possible and restrict premium differentiation to causal conditions that are acceptable to the general public to enhance their social profile.

Well-designed product differentiation is crucial from an economic point of view, companies that manage this balancing act well will profit from these additional chances to reposition themselves in the current shake-up.

We at SCOR are not only happy to work with our clients in understanding and quantifying the extent of some of the implications, but also help them benefit from the upcoming changes through our support in pricing, product development or tailor-made reinsurance solutions.