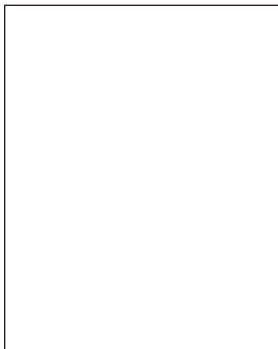


# The Legal Expenses Insurance Directive – a consumer perspective<sup>1</sup>

by juris kandidat **Klaus Ilmonen**

---



This article studies the implications of the Legal Expenses Insurance Directive for consumers in Europe. Even if the directive includes interesting elements with regard to the development of consumer and private law in Europe, it reveals more about how directives are instituted in the EC: The author, Klaus Ilmonen, holds a Master of Laws degree and works as a lawyer in Helsinki.

*Klaus Ilmonen*

## Introduction

Legal expenses have often been seen as a factual hinder for people to carry claims through the proceedings of a court of justice. Consumers acting as plaintiffs may have an economically relatively small claim, which from a legalistic point of view should be tried by a court. But where expected legal expenses are seen to exceed the claim, the interest to take the case to court decreases even if there are relative chances of success<sup>2</sup>. Losing the case would lead to the plaintiff carrying not only the burden of the material outcome of the case but also his legal expenses as well as the legal expenses of the opponent<sup>3</sup>. The result of a comparison between suffering an injustice and taking the risk involved with court pro-

ceedings may often be that the risk is not worth taking. Even where there are substantial economic interests involved and a determination to try a case, the economy of a private citizen may not allow taking a case to its end. In England it has been found that most people may find out of court settlements far more inviting if faced by a David-Goliath claims battle with large corporations with access to any sort of legal consultation<sup>4</sup>. In any case, such a claims battle would not easily fulfil the principle of equality of arms in court proceedings.

The aforementioned leads to a factual limitation on access to justice. On a European level the question of access to justice has been seen as paramount as far as consumer interests are concerned<sup>5</sup>. The European Commis-

sion has prepared a consultative Green Paper<sup>6</sup> on consumer access to justice and included several problems raised by the increasing amount of cross-frontier trade involving consumers. In the second Community three-year action plan<sup>7</sup> concerning consumer interests the problem is given special attention<sup>8</sup> as transfrontier disputes often involve higher costs, longer duration and greater complexity of procedures<sup>9</sup>. There is still a need to develop procedures to aid the consumer to actualize his interests and rights. At this point in time, however, the problems relating to proper access to justice for consumers still remain, especially considering the costs of litigation.

Where there is risk, there often is insurance. It has been possible for quite some time for consumers to insure future legal expenses. This insurance form provides for a possibility to – by private means – guarantee a level of access to justice. The material contents of legal expenses insurance contracts have been regulated on an EC level by a Council Directive<sup>10</sup> the object of this study. The insurance form as such and as amended by the directive raises consumer-related questions which shall be studied in this presentation. Even if consumer interests may not have been an issue when the directive was developed, the directive has some impact on consumer-related issues as will be seen hereunder.

The purpose of this study is to evaluate the significance of legal expenses insurance for consumers and to study the effects of the Legal Expenses Insurance Directive on consumers within the EU<sup>11</sup>. How the Legal Expenses insurance Directive, when seen from a consumer point of view, fits in and compares in the field of EC consumer law and policy, will also be studied.

### **Definition**

---

Legal expenses insurance can be defined as an insurance providing for the possibility for

the insured to carry into effect his legal interests by covering the expenses of legal proceedings as far as legal counsel or trial fees are concerned<sup>12</sup>.

On an international level legal expenses insurance can be divided into two main sections according to the procedure in which the claim based on the insurance is managed<sup>13</sup>. In the Central European model the insurance company assesses the case of the insured, gives recommendations on appropriate measures in light of the probable outcome of the case and even advises counsel if the case goes to trial<sup>14</sup>. In the Nordic model the insurance company does not study the material side of any case but compensates all legal expenses if the case fulfils the insurance contract terms<sup>15</sup>. Even if these two categories can be specified the development of legal expenses insurance in the European countries has varied greatly. This variation has been found to depend on the varying legal systems, different codes concerning judicial procedure and specific regulation of the insurance trade in the different countries<sup>16</sup>.

Typical situations where legal expenses insurance have been used in Nordic countries are real property related proceedings (Sweden and Finland<sup>17</sup>). In Germany proceedings effected by traffic accidents and other motor vehicle related situations have been the most frequent<sup>18</sup>. Generally motor related insurances seem to be most commonly used<sup>19</sup>. This tendency seems natural due to ever increasing traffic and the often substantial economic interests involved in traffic accidents. Although the insurance form in question has been available in Europe since early in the century, it has only recently evolved into a relevant market in many parts of the continent. The first legal expenses insurances were offered in Sweden in 1961<sup>20</sup>, in Finland in 1968<sup>21</sup> and in England as late as 1974.<sup>22</sup> In England there are some six million policy holders<sup>23</sup>, but the numbers are expected to

grow rapidly. Indeed the insurers see the 1990's as the decade for significant growth in this market<sup>24</sup>.

### **Significance of Legal Expenses Insurance for Consumers**

In England some feel that the in their opinion antiquated legal system has to change and indeed will do so and that legal expenses insurance will have a significant impact on the process of development<sup>25</sup>. It is argued that with this development, the public will become more litigation conscious and will have to "look after themselves"<sup>26</sup>. Insurance would then be ideal as a security for unforeseen legal expenses rather than an instrument which would substitute legal aid<sup>27</sup>. It seems that especially in countries such as England, where it can be said that the access to justice is expensive, legal expenses insurance may be crucial to consumer interests. It seems that the use of this insurance form depends on the structure of the national legal system. In countries where institutionalized consumer protection is less developed, legal expenses insurance acts as a protective measure guaranteeing access to redress against consumerate injustices. In the Nordic countries it seems that the insurance form in question provides a possibility for the insured to actively carry through economic interests; thus the profile of the kinds of consumers who actually use their legal expenses insurance in the Nordic countries would fit people of some affluence and with medium level income<sup>28</sup>.

### **The Directive on Legal Expenses Insurance**

The relevant parties to the legal expenses insurance system have shared the opinion that "there is a need for more regulation to prevent abuses and to ensure that enough information is provided before a policyholder decides which (insurance) option to go for"<sup>29</sup>.

The EC has regulated the legal expenses insurance market with the means of a directive dating from 1987, which was to be applied in the member states as of July 1990<sup>30</sup>. The directive provides for added information to the insured as well as some absolute minimum protection concerning the material terms of the insurance contracts.

The Legal Expenses Insurance Directive applies to consumers and businesses alike. Some limitations to the applicability of the directive have been included in the directive itself<sup>31</sup> or have been allowed to be set by member states<sup>32</sup>. The scope of this study does not allow for further study of these limitations.

### **Background of the Directive**

The origins of the directive go back as far as 1973 and the so called first non-life insurance directive<sup>33</sup>. The then Federal Republic of Germany had made a reservation concerning the right of establishment of insurance companies to the effect that compulsory special-ization from companies carrying legal expenses insurance was demanded. The German regulation was intended to guarantee that no conflicts of interests would arise between the insurer and the insured which could lead to undue pressure from the insurer to force the insured for example to early settlements.

In an EC internal market the aspect of conflict of interests in legal expenses insurance contracts was relevant at the time when the directive was drafted. In most countries the insurer would estimate the probable outcome of legal proceedings concerning the insured. Where the winning chances were seen to be slight the insurer would recommend settlement or other appropriate solutions<sup>34</sup>. It would in any case be normal procedure in many member states to "conduct in-house treatment of the relevant case" before the involving of an attorney or outside lawyer became

imminent in the legal proceedings<sup>35</sup>.

It seems that the actual motive for the directive is to facilitate freedom of establishment as prescribed by the Treaty of Rome. If Germany was to approve new arrangements which would hinder conflicts of interests, the German insurance markets would be open for all EU insurance companies<sup>36</sup>. Earlier insurance companies which wished to establish themselves in the German market had to create separate subsidiary companies specialized in legal expenses insurance, thus adding costs and trouble<sup>37</sup>.

### **The Purpose of the Directive**

The Directive expressly sets out to "facilitate the effective exercise of freedom of establishment" and hinder problems related with conflict of interest where legal expenses insurance is concerned<sup>38</sup>. Such conflicts of interests may arise if the insured has other insurances with the same insurer or if another party involved in the claim where legal expenses might accumulate is insured with the insurer whether for legal expenses or other losses. An example of a possible case can be presented here: A motorist is alleged to have caused an accident while under the influence of alcohol and has both liability insurance and legal expenses insurance with the same insurer. Under such policies in general the insurer may reclaim damages from the motorist if the accident was caused by criminal activity (drunk driving). In this situation a conflict of interests has arisen and there may be valid doubt as to whether the insurer wholeheartedly is willing to defend the motorist's interests against criminal charges<sup>39</sup>. The situation above would be typical of an insurance contract in accordance with the Central European model of legal expenses insurance. Where the claims are managed by the insurer internally, the objectivity of the management can with reason be questioned.

### **Three Alternative Models for National Implementation**

The Directive offers three solutions for hindering conflicts of interests in national implementation of the directive. The solutions are seen as equal alternatives, all of which are considered to safeguard the insured "in an equivalent manner under (the) (D)irective"<sup>40</sup>. Firstly member states may guarantee the insured person the right to "entrust the defence of his interests, from the moment that he has the right to claim from his insurer under the policy, to a lawyer of his choice." To no great surprise this solution has won much support among lawyers<sup>41</sup>.

The moment from when claims can be presented to the insurer has been defined further as the moment when an insured occurrence – as prescribed by the insurance contract terms – has taken place<sup>42</sup>. Such insured occurrences may be the arising of a dispute between the insured and another party or where criminal matters are concerned, the alleged criminal act which leads to the summoning of the insured<sup>43</sup>.

In England it is common practice that the insurer advises the lawyer chosen – even if the choice has been made by the insured<sup>44</sup>. This practice may be in conflict with the requirements of the directive. Article 4 (a) states that the insured may freely choose counsel to "defend, represent or serve the interests of the insured person in any inquiry or proceedings." This wording suggests that the lawyer should only represent the insured person. Considering the special nature of the relationship between a lawyer and his client this issue is of some significance<sup>45</sup>. In Germany it has been pointed out that where a lawyer is to represent the insured under legal expenses insurance cover, the lawyer is to act solely in the interests of the insured<sup>46</sup>. Any influence from the insurer in his relationship could easily be seen as to make possible undue

influence where a conflict of interests has arisen.

According to some group policies the insuring entity, e.g. employer or professional organization, has the right to choose counsel even for the insured. This practice has been found to be in contradiction with the principle of free choice of counsel<sup>47</sup>. The only exceptions found to the freedom of choice are situations where the insured is not available to protect his interests. In German practice an insurer may in such cases act in the interests of the insured and nominate counsel to act on the behalf of the insured<sup>48</sup>.

Harbauer stresses even here that the relevant lawyer-client relationship even in such cases is to exist between the insured and the appointed attorney.

The other solutions are aimed at guaranteeing objective management of the legal expenses claims by the insurer. A member state may then alternatively require that legal expenses insurance is carried out by a separate legal entity, the relevant staff of which is not to carry on similar activities in any other insurance company (e.g. group companies) at the same time<sup>49</sup>. It is even satisfactory for the member state to require that insurance company staff involved with the management of legal expenses claims do not simultaneously carry on management of other classes of insurance<sup>50</sup>. This solution should also guarantee objective management of legal expenses claims even if management of claims is not carried out by a different legal entity.

It should be noted here that when a case has reached the point where a lawyer (or other qualified person) is needed to defend, represent or serve the insured in an inquiry or proceedings, the insured shall always have a right to choose that person<sup>51</sup>. The effect of this stipulation will be studied more thoroughly further on.

A member state may also leave the choice between the three alternatives to the insurers

and allow any of the three options. A member state may not, however, demand compulsory specialization. It may not hold, that any insurer carrying legal expenses insurance may only carry such insurances<sup>52</sup>. This policy, if enforced in the community area, would have lead to a split-up of a number of composite undertakings<sup>53</sup>.

### **Critique of the Implementation Models**

---

In England the Law Society argued that there is an inherent conflict of interest between the insurer and the insured in legal expenses insurance. The desire of insurance companies is naturally to keep costs down in all situations which may lead to the insurer pressing for early settlement of the claim, especially in situations where the insured does not have an independent and objective legal counsellor. The Law Society states that the only way to ensure that a conflict of interests does not lead to the insured not having thorough access to justice is to guarantee free choice of lawyer for the insured "from the moment the right to claim is established."<sup>54</sup>

However, the implementation in England resulted in allowing insurance companies to choose between the three solutions provided by the directive. When this choice was made, the Department of Trade and Industry (DTI) answer to the Law Society critique was that "it (did) not want to harness or impede progress in what it (regarded) as 'a major growth area'."<sup>55</sup> If insurance companies can choose between different means and consumers, and other insured can choose between insurance companies, it is the market that ultimately controls which solution is the most efficient. In any case the DTI saw no risk in any of the three solutions offered by the directive<sup>56</sup>.

The Law Society further criticized the implementation alternatives which only require objective management of legal expenses in-

insurance claims. The Law Society held that these do not sufficiently protect the interests of the insured. The arrangements are not thought to protect the insured "from the insurer's desire to keep costs down and press for early settlements to claims."<sup>57</sup> Insurers will try, whatever the internal administrative arrangements may be, to keep their costs down. When the two "administrative alternatives" allow for in-house consultation when claims are presented to the insurer, the Law Society view is that the staff of the insurer "are likely to have the interests of the insurer as their first priority and are unlikely to act in the best interest of the insured."<sup>58</sup> German authorities on the subject have presented further doubts. Whatever administrative solutions are adopted in the insurance company, the possibility (and suspicion) that there may be cooperation between the legal expenses insurance claim managers and other departments cannot be eliminated<sup>59</sup>. It is argued further that such administrative solutions could not be seen to fulfil the requirements of trust between the insurer and the insured which is considered to be a specific key element in an insurance contract relationship<sup>60</sup> in most European legal orders.

The Law Society in England is concerned not only with the specific situations of conflict of interests between the insurer and the insured as defined by the Legal Expenses Insurance Directive, but also take the view that there is an inherent conflict of interests between the two parties. It is clear that effective and extensive litigation is costly and that it is in the insurer's interest to reduce those costs, especially if the success of the case is in the least doubtful. The Law Society claims that problems related to this contractual relationship can effectively be hindered only by accepting that the insured may freely choose counsel from the moment the right to claim under the policy is established.

Insurers who do not allow for free choice of

counsel often provide for a panel of lawyers from which counsel can be chosen. The panel may include lawyers who specialize in the kinds of cases which are covered by the specific insurance policy (e.g. motor vehicle-related cases or professional liability cases). When legal expenses are add-ons to more specific combination policies it may be effective to allow limitations in the choice of counsel. Even the directive has excluded certain motor vehicle-related policies from the scope of free choice of counsel<sup>61</sup>.

It could be argued that the right to free choice of counsel could be limited in special circumstances without significantly affecting the real interests of the insured. However, it seems clear that the alternatives presented in the directive where objective management of claims is used to hinder conflicts of interest are not in the best interest of the insured. It could have been a better solution to extend the allowed limitations to the right of free choice of counsel to cover specific insurance policies where specialized counsel could effectively and economically handle cases that have been claimed under the policy. Such procedure could even have been limited to situations where the economic interests of the insured are relatively small. The directive may then not have allowed for alternative implementations. This arrangement, if properly developed, would not have had significant economic impact as it allows for limitations to the freedom of choice of counsel where such are found suitable, thus also limiting costs of litigation.

### **Material Requirements set on Legal Expenses Insurance Contracts**

---

Even if the main concern of the Legal Expenses Insurance Directive is to hinder situations of conflicts of interest, the directive is also concerned with protecting the insured in

other respects as well. The directive mainly sets out a minimum of information which is required to be given to the insured when a legal expenses insurance contract is entered into. This added information to the insured is in accordance with EC policies on consumer interests as it is seen that an enlightened consumer can make better judgments through thorough information being available<sup>62</sup>. Direct interventions in the contractual relationship are made as well, as shall be seen below.

The directive requires that a legal expenses insurance contract be entered into as a separate contract or as a separate section in a combined policy. In any case the nature and conditions of the legal expenses insurance shall be specified for the insured in the contract<sup>63</sup>. This requirement to inform the insured, when applied to group policies where the insured generally do not receive a separate written insurance, leads to that a written statement on the central nature of the legal expenses insurance cover should be submitted to each insured person<sup>64</sup>.

If a member state adopts the solution of requiring that the management of the relevant claims be entrusted to a separate legal entity, that undertaking shall be mentioned in the clauses defining the nature of the insurance contract. If the alternative of free choice of lawyer is adopted, the insurance contract must include express mention of this right of the insured<sup>65</sup>.

Furthermore, the contract shall include the right for the insured to consult a lawyer of his choice<sup>66</sup> and to have recourse to an objective arbitration procedure when a conflict of interests emerges between the insurer and the insured<sup>67</sup>. At this time the insurer is to specifically inform the insured of these rights<sup>68</sup>. Such a situation could emerge i.e. when there is a difference of opinion on whether a case should be settled or taken to court<sup>69</sup>.

As stated earlier the insurer shall have the right to choose counsel freely when actual

judicial proceedings are imminent even if national legislation allows the insurer to manage a case initially. The insurance contract shall "expressly recognize" this right of choice, and an insured person may now be certain that a lawyer of his own choice will ultimately handle the case to its end. The problem to be solved is when this moment is at hand. The Law Society in England argue that the decision to issue proceedings may be crucial for success. There should also be continuity between preparing a case and taking it through legal proceedings<sup>70</sup>. This directive stipulation has a significant impact on legal expenses insurance contracts in Europe. It can be said that the core-handling proceedings – of the contractual relationship has been altered by the directive. The common practice in accordance with the Central European model for the insurers to deal with the cases themselves will be affected to this extent. However, in smaller cases it could well be in the interest of the insured to accept a lawyer recommended or chosen by the insurer<sup>71</sup> as such lawyers may have routine with dealing with the kinds of cases where the legal expenses insurance contract applies, e.g. in motor related insurances<sup>72</sup>.

While the Legal Expenses Insurance Directive addresses several consumer problems relating to insurance contracts, many problems are left to national legislation or to the discretion of the insurer. The insurer may naturally set maximum costs that the policy covers. If these cost limits are too low, it will obviously limit the right to choose counsel. If, on the other hand, there would be unlimited freedom of choice of counsel and very high cost limits, the insurance would not be profitable for the insurer. This comparison of interests should be studied in the light of the three alternative models of hindering conflicts of interest. It seems even in this aspect that where the policy is specific as to the nature of the risk, the freedom of the choice of

lawyer could be limited without compromising the interests of the insured. The insurer could use specialist lawyer panels who, at a low cost can effectively and objectively handle the specific kind of cases. However, legal expenses insurance contracts of a more general nature require more freedom for the insured to choose counsel.

### **The Unfair Contract Terms Directive and Legal Expenses Insurance**

The Legal Expenses Insurance Directive provides the framework for the legal expenses insurance business. It also provides limits for allowed clauses in legal expenses insurance contracts. However, the individual consumer contracts concerning legal expenses insurance also fall into the scope of the Unfair Contract Terms Directive<sup>73</sup>. This directive stipulates which contract terms are to be considered to be unfair from the consumer point of view and thus inapplicable and void in the individual contract relationship. It can be stated here that insurance companies in England have been forced to amend their standard contract terms concerning legal expenses insurance contracts to meet the requirements of the Unfair Contract Terms Directive<sup>74</sup>.

The preamble of the Unfair Contract Terms Directive sets a limitation on the applicability of the directive on insurance contracts:

“whereas it follows, inter alia, that an insurance contract, the terms which clearly define or circumscribe the insured risk and the insurer’s liability shall not be subject to such assessment since these restrictions are taken into account in calculating the premium paid by the consumer.”

This means that insurance companies can completely exclude certain risks from the scope of the insurance. This is also common practice even concerning legal expenses insurance<sup>75</sup>. For example in the combined home

insurances all risks relating to employment relations or trade of the insured may be left outside the scope of insurance coverage<sup>76</sup>. Insurance companies as a rule do not cover legal expenses concerning matrimonial relations, building work, letting and libel<sup>77</sup>. Other usual exclusions include investments and company shareholding<sup>78</sup>. This basic limitation may thus even lead to the exclusion of coverage for the most common consumer risks.

It can be concluded here that the Legal Expenses Insurance Directive includes rather specific stipulations that protect the insured in relation to the insurer. The problems specific to legal expenses insurances (i.e. conflict of interests, undue influence) are directly dealt with by the directive itself as are some procedural problems as seen by the above comparison. When adding the applicability of the Unfair Contract Terms Directive to legal expenses insurance contracts one can see the scope of regulatory intervention in this specific contractual relationship as well as the level of protection of the insured. Where the Legal Expenses Insurance Directive and the Unfair Contract Terms Directive coincide it seems that this level is satisfactory. However, many problems related to legal expenses insurance have been left unsolved.

The limitations of applicability concerning insurance contracts included in the preamble of the Unfair Contract Terms Directive seem to allow for a wide range of limitations as to the risk carried by the insurance policy. Thus the insurer is free to exclude any situation from the coverage. The Legal Expenses Insurance Directive allows for different alternative national implementations which directly affect the nature of the contract. Furthermore, there are few restrictions concerning limitations of insurer liability, i.e. exclusions of risk, thus allowing for even further variety in insurance contracts. Even within one member state there may then be contracts with



totally varying coverage the total scope of which can be very difficult to establish<sup>79</sup>. It has been argued that legal expenses insurance contracts have been harmonized in Europe through legislation, and that by definition no great variety should exist in the material side of the contracts<sup>80</sup>. A conclusion to be drawn from the presentation above, however, is that the level of consumer comparability concerning legal expenses insurance contracts is not on a particularly high level.

### **The Legal Expenses Insurance Directive and EC Consumer Policy**

---

It has been argued that the Legal Expenses Insurance Directive, though adopted before the Single European Act came into force<sup>81</sup>, can perhaps be seen as an early manifestation of the 1992 spirit<sup>82</sup>. It is therefore meaningful to study what statement the directive makes as far as the development of EC consumer policy is concerned.

Even before the latest developments in the integration process, consumer issues were a part of EC law. For example in the case *GB-INNO v CCL*<sup>83</sup> the European Court of Justice found that consumers have a right to participate in the process of market integration and emphasized that there is a close connection between consumer protection and consumer information<sup>84</sup>. Through the Maastricht Treaty, the elevation of consumer protection to the status of Community common policy has been confirmed<sup>85</sup>. According to the Maastricht Treaty<sup>86</sup>, the Community shall contribute towards a high level of consumer protection through directives, for example, in order to protect the economic interests of consumers and in order to inform consumers. With the Maastricht Treaty the pursuit of consumer interests has become independent from the development of the internal market<sup>87</sup>. The social dimension of the EC can be seen to

have been strengthened by the new adopted policy.

The Legal Expenses Insurance Directive provides for extensive information to be given to the insured. This added information is relevant in daily use of insurance policies as it has even been found that consumers can be unaware of that they have insurance cover for a specific risk altogether and completely ignorant of the detailed terms of the insurance policies and thus of their rights according to those policies<sup>88</sup>. The issue of access to justice has been seen to be a major concern within the EC and an important aspect to be noted in the integration process. The development of consumer access to justice has not reached any consumer ideals at this point and the legal systems remain rigid. The Commission Green Paper<sup>89</sup> even states that "(t)he problems of access to the courts which the creation of a European area will pose are far from having been resolved. If there is a dispute, the single Market will be replaced by 12 – or even more legal systems, all jealous of their independence and sovereignty." The Legal Expenses Insurance directive provides for a possibility for consumers to improve access to justice in the prevailing somewhat rigid legal systems.

EC regulation in the insurance sector has been aimed mostly at opening the insurance markets within the EU according to Reich<sup>90</sup>. Consumer protection has been limited to conflict-of-law rules and a certain level of improved information to the policy holders.

Legal expenses insurances were regulated on an EC level mostly in order to open up markets. However, in the process some extensive safeguards essentially of a consumer protection nature were included in legal expenses insurance contracts<sup>91</sup>. In this context it is significant to note the requirement that an insured always has free choice of counsel when actual legal proceedings commence. This directive stipulation intervenes materially in the contractual relationship and repre-

sents a more developed form of protection of the insured. These stipulations, as they intervene in the contractual relationship, can be seen to establish, that consumer protection concerning legal expenses insurance may be on a higher level than in insurance contracts in general as far as EC contractual regulation is concerned.

Generally the protection of consumers in the EU has been executed by consumerspecific legislation. The consumer law of the EC concerning consumer contracts has been strictly differentiated from general contract law<sup>92</sup>. In the case of legal expenses insurance the regulatory intervention in contract law is generally applicable (partially due to the special background of the Directive) thus bringing forth a general concept of protection of the weaker contracting party within this specific contract form. In that aspect the Legal Expenses Insurance Directive does not seem to follow the common tendency towards consumer specific legislation. However, the directive only covers a specific insurance form and has a very specific background.

### **Conclusions**

---

In states where consumer interests are not institutionally represented, the insurance is used in order to take legal action even regarding consumer rights. In the Nordic countries the insurance form has allowed consumers to actively use the justice system to their economic advantage. Here it seems that the equality of arms-principle is best achieved. In most countries, however, the insurance has been successfully used to cover unexpected legal expenses relating to accidents and other unforeseen events.

While one specific use of the insurance does not seem to dominate, it can be concluded that different consumer related interests can be protected and represented through legal expenses insurance. Considering the low cost

of the insurance as an add-on to common policies, this insurance seems to have a prominent place in European insurance trade.

The Legal Expenses Insurance Directive provides minimum standards as far as legal expenses insurance contracts are concerned. The standards mostly express EC consumer policy, emphasizing consumer information. However, the contractual relationship is also directly affected by absolute stipulations mainly of a consumer protection nature. The Directive guarantees that ultimately the insured may consult a lawyer of his choice (when legal proceedings are to commence). This stipulation has the most significant effect on legal expenses insurance contracts on a European level as it changes the core of the Central European model of legal expenses insurance.

Unfortunately the directive does not address many relevant questions relating to the insurance policies. The insurer can freely exclude risks from the scope of the policy as far as the directive is concerned. Even if this leads to a significant imbalance in the contractual relationship, neither the Legal Expenses Insurance Directive nor the Unfair Contract Terms Directive provides protection for the insured. The problem is not only theoretical as limitations of risk are customary in legal expenses insurance. Another relevant problem is raised by the alternative implementation models concerning hindering situations of conflict of interests. It is possible that policies where different solutions have been used to hinder conflicts of interest are offered on the same market and in the same member state (e.g. England). As such policies are different to their nature and in addition can include varying limitations of risk and cost and different premiums, this leads to difficulties in comparability of legal expenses insurance policies.

More than anything else, the Legal Expenses Insurance Directive portrays how directives

are instituted by the EC. There can hardly be any doubt that the directive is a compromise as are many newer regulatory instruments of the EC<sup>93</sup>. Its main implicit purpose is to open up the insurance markets in Germany for European insurance companies. In the process Germany has managed to extend some national standards to cover the EU. It seems that the reservation made by Germany concerning the right of establishment of insurance companies<sup>94</sup> has forced the EC to adapt a level of (consumer) protection in the field of legal expenses insurance more or less equal to the protection in Germany. There has been no sign that there was any other particular need to harmonize legislation in this area than to gain access to the German market for European insurance companies. This could be seen as a case where the more powerful market areas (states) may set standards within the EU. From a Nordic perspective this tendency has been noted with some concern. In some matters the perspective taken to consumer protection in the Nordic countries differs from a European approach of supporting market efficiency<sup>95</sup>. Even the adopted basic views held on these issues may be altered by an integration process, that is based on the influence of strong markets.

The alternative implementation models presented by the Legal Expenses Insurance Directive express the interest of member states to preserve status quo. The models seem to a high degree to allow traditional practices in member states. Firstly the free choice of counsel model corresponds with Nordic traditions concerning legal expenses insurance. Secondly the model where legal expenses insurance is to be carried out by a separate legal entity is very close to the status of affairs in Germany. Lastly the model requiring objective handling of a legal expenses insurance claim within an insurance undertaking seems to guarantee a minimum level of protection of the insured. The models concentrating on the

objectivity of the administrative procedures of the insurer cannot actually be seen to guarantee the same level of protection of the insured from undue influence of the insurer as the model of free choice of counsel. The administrative models could have been replaced by specified limitations to free choice of counsel, as shown earlier in this study, without compromising the economic interests of the insurer. It seems that the member states have been more concerned with preserving status quo than with the actual economic impacts of the stipulations of the directive.

It seems that when the directive was instituted, some concern was shown regarding existing community consumer policies. Mainly policies concerning added consumer information have been portrayed in the directive in accordance with consumer policy in the insurance trade in general. Furthermore, the possibility to exclude risks in insurance contracts – specifically used in legal expenses insurance contracts – undermines the assumed consumer protection-nature of the Legal Expenses Insurance Directive. Such possibilities to limit risks can mostly be seen to further the interests of insurers.

It can be stated that the minimum requirements of the directive are only partially related to an actual will to protect the insured in legal expenses insurance contracts. The directive, in form and content, reveals that pressure to meet German standards has been of paramount importance when the level of protection has been stipulated.

## Notes

<sup>1</sup> This article is based on a thesis for the juris kandidat-degree at the University of Helsinki. The thesis was a part of the project "Marknadsföring och kontrakt i EG-rättsligt perspektiv" under Professor Thomas Wilhelmsson.

<sup>2</sup> Viitanen, p. 437

- <sup>3</sup> Eg in Finland the judicial code has recently been amended to the effect that the responsibility of the losing party to cover all the legal expenses of the opposing party has become more absolute.
- <sup>4</sup> The Times, 1.11.1994
- <sup>5</sup> The consumer right to proper redress for injury and damages was one of five categories of consumer rights defined in Council Resolution of 14 April 1975 (Programme for a consumer protection and information policy), OJ 1975 C92, Kendall, p.156.
- <sup>6</sup> Commission of the European Communities: Green Paper on the Access of Consumers to Justice and the Settlement of Consumer Disputes in The Single Market, Brussels, 16 November. 1993
- <sup>7</sup> COM (93) 378
- <sup>8</sup> Haverinen, p.97
- <sup>9</sup> Kendall, p.158
- <sup>10</sup> 87/344/EEC: Council Directive of 22 June 1987 on the coordination of laws, regulations and administrative provisions relating to legal expenses insurance
- <sup>11</sup> In this presentation the term EC will be used for all regulatory instruments and institutions of the European Communities. Any reference to the EU will refer to the geographical area (states) covered by the Maastricht Treaty.
- <sup>12</sup> Arti, 1985, p.10; In the English Insurance Contract Act from 1982 this insurance form is defined as "effecting and carrying out contracts of insurance against risks of loss the persons insured attributable to their incurring legal expenses (including costs of litigation)", Merkin, p.B.9.7-02
- <sup>13</sup> Hynynen, LML 1.11.1995, p.1
- <sup>14</sup> H.Grundy, Law Club Legal Protection, 2.11.1995
- <sup>1</sup> Hynynen, LML 1.11.1995, p.1
- <sup>16</sup> Oikeusturvatoimikunnan mietintö, p.5
- <sup>17</sup> Hynynen, LML 1.11.1995
- <sup>18</sup> Nousiainen, p.114,118-119
- <sup>19</sup> Hoppu, p.39
- <sup>20</sup> Lidman, p.146
- <sup>21</sup> Government Bill HE 137/93,p.3
- <sup>22</sup> The Legal Executive Journal, January 1988, John C. Vann, FCII
- <sup>23</sup> Approx. 7% of the British population is covered by legal expenses insurance, Legal Expenses Insurance in the UK, Report 1991
- <sup>24</sup> The Legal Executive Journal, July 1990
- <sup>25</sup> Allianz Cornhill Legal Protection Insurance Co. Ltd in The Legal Executive Journal July 1990
- <sup>26</sup> The Law Society's Gazette Nr. 18,1990, p.7
- <sup>27</sup> The Law Society's Gazette Nr. 18,1990, p.7
- <sup>28</sup> Hynynen, LML 1.11.1995
- <sup>29</sup> The Law Society's Gazette Nr. 18,1990, p.7
- <sup>30</sup> Article 10
- <sup>31</sup> Preamble to the directive 87/344/EEC
- <sup>32</sup> Article 5
- <sup>33</sup> Directive 73/239/EEC of 24 July 1973 on the coordination of laws, regulations and administrative provisions relating to the taking-up and pursuit of the business of direct insurance other than life assurance.
- <sup>34</sup> Finnish Government Bill HE 137/93,p.4
- <sup>35</sup> Pool,p.26
- <sup>36</sup> Finnish Government Bill HE 137/93,p. 3-4
- <sup>37</sup> Pool, p.26
- <sup>38</sup> Article 1
- <sup>39</sup> Pool, p.25
- <sup>40</sup> Article 3.3.
- <sup>41</sup> Law society Response to the Consultation Document on Legal Expenses Insurance, p.1
- <sup>42</sup> Swedish Government Bill, Regeringens Proposition 1992/93:257, p. 140; Hoppu, p.55
- <sup>43</sup> Hoppu, p.55; Hynynen argues, however, that the moment when claims can be presented to the insurer is when a summons is presented to the insured, LML 1.11.1995, p.3.
- <sup>44</sup> H. Grundy, Law Club Legal Protection, 2.11.1995
- <sup>45</sup> Harbauer, p.400-402; A detailed study is presented of the problem of the three involved parties in legal expenses insurance relations.
- <sup>46</sup> Harbauer, p.401
- <sup>47</sup> Decision of the Supreme Court of Germany, 1990, reference in Suomen Asianajajaliiton lausunto, p.5
- <sup>48</sup> Harbauer, p.400
- <sup>49</sup> Article 3 (b)
- <sup>50</sup> Article 3 (a)
- <sup>51</sup> Article 4 (a) and Pool, p.26
- <sup>52</sup> Article 8
- <sup>53</sup> Preamble to the Legal Expenses Insurance Directive 87/344/EEC
- <sup>54</sup> Law Society Response to the Consultation Document on Legal Expenses Insurance, p.4
- <sup>55</sup> The Law Society's Gazette Number 18 Wednesday 16 May 1990, p.6
- <sup>56</sup> The Law Society's Gazette Number 18 Wednesday 16 May 1990, p.6; Department of Trade and Industry (DTI): Consultative Document on Legal Expenses Insurance, p.6
- <sup>57</sup> Law Society Response to the Consultation Document on Legal Expenses Insurance, p.3
- <sup>58</sup> Law Society Response to the Consultation Document on Legal Expenses Insurance, p.4
- <sup>59</sup> Werner, p. 253; reference to quote from Prof. Hans Möller in Zeitschrift für Versicherungswesen 1969,

- p.777: "beim Versicherten der Verdacht der Zusammenarbeit der Abteilungen nicht beseitigt werden kann"
- <sup>60</sup> Werner, p.253
- <sup>61</sup> Article 5; The origin of the exclusion is the practice of popular motor clubs in Central Europe. It has been found that the cover provided by those policies is effective. .
- <sup>62</sup> Reich, p.99, with reference to added information requirements on the third non-life insurance directive 92/49/EEC
- <sup>63</sup> Article 3.1.
- <sup>64</sup> Government Bill HE 137/93,p.6
- <sup>65</sup> As a point of interest it can be stated here that some Finnish insurance contract terms studied in connection with this presentation did not fulfil this requirement.
- <sup>66</sup> Article 4
- <sup>67</sup> Article 6
- <sup>68</sup> Article 7
- <sup>69</sup> Pool, p.26
- <sup>70</sup> This problem has been noted by Law Club Legal Protection. If an insured wishes to obtain a specific solicitor the insurer is likely to accept this as changing solicitors only adds costs substantially, H.Grundy, Law Club Legal Protection, 2.11.1995.
- <sup>71</sup> Insurance companies may carry panels of lawyers from which the insured can choose one, H. Grundy, Law Club Legal Protection, 2.11.1995
- <sup>72</sup> The Lawyer, 6 April 1993
- <sup>73</sup> Council Directive 93/13/EEC of 5 April 1993 on unfair terms in consumer contracts
- <sup>74</sup> H.Grundy, Law Club Legal Protection, 2.11.1995
- <sup>75</sup> Such practice may even be considered characteristic for legal expenses insurance provided in accordance with the Nordic model, where the insurer does not assess the material side of cases claimed under the insurance, Hynynen, LML 1.11.1995, p.6. Lately all insurance companies in Finland have omitted compensation for legal expenses for a defendant in criminal cases where the prosecutor has been the plaintiff, even when the defendant has been found not guilty. This omission was done due to expected new legislation on state compensation in such cases, which has since then not been instituted. There is thus no possibility for an innocent accused to get compensation for his defense, HS 30.9.1995.
- <sup>76</sup> Finnish Government Bill HE 137/93,p.3
- <sup>77</sup> The Law Society's Gazette 18/1990
- <sup>78</sup> Legal expenses Insurance in the UK, Report 1991
- <sup>79</sup> Eg it can be difficult to compare a cheaper policy which does not allow for free choice of lawyer but covers a wide variety of cases and a more expensive policy with free choice but more limits on risk.
- <sup>80</sup> Norio, p.151
- <sup>81</sup> Pool, p.26
- <sup>82</sup> Pool, p.25
- <sup>83</sup> GB-INNO-BM v Confederation du Commerce Luxembourgeois, Case C-362/88 (1990) ECR I-667, Micklitz, Weatheriü, p.293
- <sup>84</sup> The Court drew on the Council Resolution of 19 March 1981 (Second Programme for a consumer protection and information policy), OJ 1981 C133
- <sup>85</sup> Article 3: "the activities of the Community shall include) a contribution to the strengthening of consumer protection.", Kendall, p.25
- <sup>86</sup> Articles 3 s), 100 a, 129 a and 189
- <sup>87</sup> Micklitz, Weatherill, p.299
- <sup>88</sup> LiRunen, LML 1.11.1995
- <sup>89</sup> Commission of the European Communities: Green Paper – Auess of Consumers to Justice and the Settlement of Consumer Disputes in the Single Market, Brussels, 16 November, 1993, p.12
- <sup>90</sup> Reich, p.99
- <sup>91</sup> Pool, p.26
- <sup>92</sup> Wilhelmsson. p.126
- <sup>93</sup> Paasilehto, p.416
- <sup>94</sup> Directive 73/239/EEC
- <sup>95</sup> Wilhelmsson, p.133