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Two Decades of Danish Experience on Bank-Insurance[1]

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This article reflects on the fact that bank-insurance activities began in Denmark relatively early, as an insurance driven initiative. But the basic prudential legislation was in place even earlier, and due to this, even if great problems appeared, they never caused losses to the policy holders.

As internationalisation and the EU open the market to financial conglomerates, the protection of investors, savings and consumers also begins to complete at international level, especially in the EU.

Basic protection follow from the two classical procedure areas of supervision and bankruptcy procedures. But the most important elements in any protection system is material law. This article, of course, looks into the freedoms and restrictions under financial (prudential) law. But increasingly, the protection follows from a delicate balance and interrelation between prudential law and its "parent" areas of general law of equal importance: company law, contract and consumer law, competition and data protection law, and – in high taxed countries like Denmark – tax law.

1. Introductory Remarks

The bank-insurance problems have for now nearly two decades attracted the attention of the supervisors and legislators, both from a prudential regulation and a consumer protection point of view.

Equally, it has attracted an increasing curiosity from members of parliament, and a loudspoken critical attitude on the part of consumer organisations.

At European and worldwide level, the financial conglomerates have attracted an increasing attention as it appeared that insufficient legislation and supervision threatened to rock the whole ship or to rotten the ship from within.

High marks of this interest is the worldwide collaboration on the subject between the BIS, the IAIS, and the IOSCO within the BIS framework.[2] In the EU, there already are the directives on consolidated supervision (92/30 and 98/78) and the BCCI-directive.

Also at the theoretical level the subject attracts an increasing interest. Here, however, the problem is that there are so few who

master the whole range of theoretical subjects and the supervisory skills. Therefore a relatively small contribution has come from the legal theory.[3]

For a variety of reasons, Denmark developed its legislation on financial conglomerates long before any other European state, and this advanced state of affairs lasted till well into the 1990'ties.

The starting point for this was the new Insurance Business Act of 1979. In the act was incorporated the new Companies Act 1973. But the rules on groups of companies were remodelled several times during the elaboration of the project, also taking into account the work in the EU Commission on *materielles Konzernrecht*.

When the biggest three Danish insurance company groups in the mid 1980'ties began their transformation into financial conglomerates, the new legislation passed the practical tests. Since then, the legislation and the supervisory techniques in Denmark have been constantly fine-tuned, and great practical and intellectual efforts were put into this. And twice (1987 and 1992) we had committees to reflect and report on these developments, and a third committee is now reflecting.

At the same time, Denmark built up a strong unified supervisory system.

The benefactory effect of this was, that when the two biggest insurance led financial conglomerates Baltica and Hafnia, due to bad management and financial overstreching, came into unsolvable troubles in 1992, no policy holder lost his savings or rights.

The Danish experience allows for certain practical deductions which are not always welcomed.

The first is that the most important thing is not the supervision, but the law. The law must give clear guidance for all those who want to follow the law, and to the supervisors. Without clear rules the supervisors cannot act decisively and with full moral and legal authority, nor can they, to some extend, act at all because of the requirements of the rule of law. And by "law" is meant not just the financial sector regulation, but all commercial law.

The second observation is on the nature of the law on supervision. In theoretical work and in practical drafting and supervision it is of the highest importance never to forget that banking, insurance, and securities legislation is – and is only – a supplement to the general legislation on company law, bankruptcy law, and (for insurance and securities) contract and consumer law. There are some areas where these general laws for a number of practical and political reasons are weak and too weak for financial enterprises (in fiduciary relations), notably

- on capital adequacy
- on accounting
- on dissolution procedures and the order of claims
- on fit and proper requirement, and
- on a more (pro)active/profylactic activity from the public authority than the Companies Registers can undertake.

Here, the financial legislation is a required supplement.

Thirdly, these subjects belong to the "classical" core of civil law. This is not economic policy (a supervisory authority does not make a "policy", but enforces material law by means of administrative law), nor even economic law. This is what lawyers and accountants are trained for. But in practise, the area is dominated by ministries of finance and central bank, where this fact is often not sufficiently reflected in the administrative set up.

On the other hand, this explains a part of the headline catching scandals in the financial world. And its acceptance in Denmark is a part of the explanation of the better Danish record. In fact, anything else would have been a theoretical sensation. And it should give the legal theory a special moral duty to guide the

public and the public authorities in the area.

Fourthly, the Danish experience underlines a point that is underscored in the international debate. This debate often focuses on banks for a number of reasons: Bank crashes are more spectacular and are regarded as more dangerous to the economy. Bank problems are also easier to understand, and they are short term – here and now.

Both the insurance and banking have the well known problems such as double-gearing and contagion. But in a financial conglomerate, the long term top danger is the protection of life savings. It may be that its actuarial background is insufficiently understood, it may be a desire to play with the long terms savings ”more actively to enhance production and employment””, and it may be a desire from the management or the supervisors and ministers to ”borrow” the life savings in order to avoid problems here and now in the hope that ”something will show up” long before life insurance obligations become due – and then, thanks to the intransparant nature of the life insurance, beneficiaries hopefully cannot see whether they suffered real lost thereby.

The Danish experience is, however, that if the legislation is good, and if the supervisors are ready to brave the political forces and other powerfuls, the life insurance saving may be kept out of the shipwreck. In this relation it is also of importance that the consumer protection organisations are awake and efficient.

2. The Situation Today In Denmark

2.1. Bank-Insurance Co-operation

Co-operation between banks and insurance companies have probably in some form existed for a long time, especially at the level of local banks and insurance companies, and financial conglomerates on a big scale have been known in Denmark for nearly 15 years.

Strange as it may appear today, we should not forget that the sharp competition only entered the financial world in the 1970'ties. Before that the internal codes of conduct of the financial world restricted it.

The development of express and more aggressive business strategies emerged during the 1980'ties. Today all major players on the market somehow are linked up in some alliance bank-insurance-mortgage credit. Many regard it as a condition for survival.

There was especially one area where banks and insurance companies fought bitterly for market shares: pension savings (see also 12.3 *infra*). Banks took, after amendments of tax laws in the 1970'ties, a bigger share of the non-risk savings. But on the other hand they needed to combine it with the risk products which under law only insurance companies can offer. Hence the need for permanent co-operation between a bank and an insurance company.

The insurance companies during the same period followed the same strategy by trying to link up with a bank that could present their products to potential customers. Their problem was that most people before the days of home-banking often came in their bank, but not in their insurance company – with which they only had contact to pay premium or when something sad has happened. In the bank e.g. travel insurance could be offered to those who buy foreign currency, and the bank thereby got the canvassing fees. The insurance companies thereby won many outlets and shop-windows for their products, as Denmark in the 1980'ties was heavily “overbanked” with far too many bank branches. The banks were to be compensated by becoming the insurer's recommended place for non-risk pension savings and certain loan products. But it was not always clear, if the banks and the insurance companies got an equal profit from the transaction without which alliances will experience long term problems.

The biggest insurance companies followed a double-tracked strategy, as they not only tried to combine products with some banks. They founded their own in-house banks for pension savings. This strategy is expanded a bit more in 4.2. *infra*.

The first generation of conglomerates were insurance driven. Today the picture has changed and become more varied. The two biggest Danish banks (*Den Danske Bank* and *Unibank*) both have constituted their own mortgage credit bank. *Den Danske Bank* acquired at the smelt-down of the *Baltica* Insurance group the biggest Danish life insurance company, *Danica*, and *Unibank* founded its own insurance company, *Enhjoerringen*. In addition to the biggest, some 60 of the smallest banks founded a mortgage credit bank on a special concept.

2.2. The Definition of Banks and Insurance Companies

Under Danish law, most pension funds are life insurance companies. This was accomplished by the Insurance Business Act 1979 and acknowledged by the 3rd life insurance directive, see now art. 8(1)a of the 1st life directive.

Equally, saving banks are banks with a full banking licence under the Banking Act 1974.

In the building society sector, there have been some restrictions under the Mortgage Credit Banks Act. These restrictions must be seen in the light of the special situation of Danish Mortgage Banks, including their size. The biggest mortgage bank is bigger than all commercial banks, and the Danish bond market is *per capita* by far the biggest in the world (circulating amount more than 1 trillion DKR, and the annual turn over in bonds trade approaching 10 trillion DKR). As mentioned above, some banks now have their own mortgage credit bank.

The institutions mentioned here had traditionally one problem in common. They were organised as self-owned foundations (trusts), or as mutuals, i.e. associations. The company law problems for financial groups are discussed under 6 *infra*. But pension funds have one more peculiarity. Under the general collective agreements between employers' and employees' organisations, they normally have a monopoly for obligatory pension savings in a defined part of the labour market.

3. The Legal Rules on Restrictions of Activity

3.1. The General Principle

The starting point in the world of realities is that prudential supervision requires the specialisation of financial enterprises. The most important legal reflection of this is art. 8(1)b of the 1st generation insurance directives, under which life and non-life insurance shall be pursued in companies having only this part of insurance as their social object.

The Insurance Business Act ss. 6 and 8 repeat of course these principles, and parallelly s. 1 of the Banking Act restricts the activities of banks to banking activities (as defines by the 2nd banking directive minus mortgage credit).

Because of the "balance principle" (between the amounts of outstanding mortgage credit loans and the circulating bonds), mortgage credit financed by quoted, negotiable bonds can only be carried out through specialised mortgage banks.

The requirement of a special legal entity does not, however, say anything about who may own or not own these companies. For many years this was a non-problem. The political problem was rather the inverse: May financial enterprises own shares in non-financial industrial companies. This was not primarily a prudential supervision problem. This was a political animosity towards the

insurance sector on the part of the establishment of industry.

Today the legislation permits banks and insurance companies to own each other, see 3.2. infra.

3.2. Permissible Cross-Border Activities

The question on permissible cross-border activities can be split into two: What may a financial undertaking do by itself, and what may it do by means of an affiliated daughter company.

Within its own corporate entity, the prohibition on "foreign" activity is still rather strictly enforced.

There may be some overlapping from ages old between banks and non-life companies in the guarantee area. There are also some forms of health and sickness insurance which under different names can be contracted as both life and non-life insurance.

But the development of conglomerates and co-operation alliances has removed the interest from what appeared to be the biggest problem 15 years ago, where the banks wanted to be admitted into the pension contracts with a low actuarial risk element (less than 20%). May be, tax law will reduce this further, see 12.3 *infra*.

All financial enterprises are entitled to perform also such activities as are "accessoric" to their main (licensed) activities. Such notions are fluid, and are meant to be so, and their contents vary with time

Basically, the prohibition on "foreign" activities applies also to activities carried out in affiliated companies. This principle of company law in general was established by the Supreme Court in the mid 1960'ties. However, the Banking and Insurance Acts permit an bank or an insurance company to own and control an company carrying out foreign activities, provided that it be an activity that submits the latter company to the supervision of the Danish Financial Supervision Authority, (and of course provided that the statutes of the mother company permits it).

This means in clear language that banks and insurance companies may own each other.

But ironically, this is not the site of the real problem. Perhaps more dangerous for supervisors and shareholders are the groups where the mother company is not under the financial supervision, but is a normal (mother) company or a financial holding company. Again, on a minor scale this has been known for a long time, e.g. in captive insurance, and also banks may had major industrial shareholders. But its growth and consequential problems have caused the public, consumer organisations, the supervisors, and legislators to react, cf. 1. *supra*.

4. Financial Conglomerates – Possibilities and Limits

4.1. General Requirements For Permissible Financial Conglomerates

Outside the rules described under 3 *supra* there are no restrictions, nor should there be *de lege ferenda.* This means that the requirements of the law are

- each main activity in a special company,
- each company must have its own capital adequacy, and
- transparent accounting.

However, the biggest danger revealed (outside cases of criminal activity) has been management that was not fit and proper. Sometimes, they are just not good enough, and sometimes they even believe that they and their strategic visions can walk on the water. Furthermore there is a tendency to recruit more for general skills than for knowledge of the financial sector's problems.

The somewhat discretionary, administrative

powers known in UK law against unfit or improper persons are not available to Danish authorities. Both judicial procedures and material scope subordinate them to the general principle of penal law on "resocialisation", and the European Court of Justice recognised this restriction in the *Delquist* case (1978).

It has been the tradition to regulate these problems by strict rules forbidding banks' executive directors to participate in "other" economic activities. This has worked well for banking, but utterly failed in the 1980'ties when it was transposed into insurance regulation. It was therefore abolished again for insurance, only to be reintroduced in the form of parallel and too detailed rules in the Banking and Insurance Acts in 1997.

4.2. Ownership Problems

The first generation of bank-insurance in Denmark was virtually totally insurance driven. The reason was the volume disease, the need felt by the insurance industry in the 1980'ties to expand, and not to let the banks run with a big part of the pension savings. The other part was the wish of avoiding to pay external banks all the handling costs and fees in case of investments.

The needs of the banks to expand into insurance, and especially life insurance, was for much the same needs. Further the banks like to have the kind of long-term money which life insurance savings constitute in their full control.

Behind this is also a concept evolving during the 1980'ties: the "total client" concept where the client has relations to only one financial enterprise. This should give "synergy advantages" to both parties, and certainly to the financial conglomerate.

On a technical level, it should be noted that banks may not only *acquire* insurance companies, and vice versa. They may also found them, and build them up from scratch. The latter is as frequent (and they have no starting capital problems).

Finally it is recalled that financial groups are submitted to special consolidated accounting and supervision and to additional capital adequacy rules. Also in company law there are special limitations, e.g. on loans to shareholders, see 6.2 *infra*.

5. The Organisation of Cross-Frontier Distribution

5.1. Prudential Law Restrictions?

Basically there are no limits to banks' and insurance companies' distributing each others products, as long as this is "ancillary" or "accessory" activity (or done through an affiliate company). These notions are "legal standards" which are being given substance from tradition and practise of the companies, the supervisors, the courts, and the contractual practise. Their contents thus vary with time.

Presently there are not many product limitations. Eventual restrictions would rather stem from other areas such as consumer or data protection law. The only prudential restrictions that can be identified out are those that follows from the fact that the banking and insurance product must, for reasons of capital adequacy calculations, be clearly separable from each other and other products. But it also follow from consumer law.

It follows, however, from the very notions that any such distribution activity must be quantitatively "ancillary" or "accessory". This means that the primary activity of banking or the agreement's classes of insurance must be bigger and so big in comparison to the "ancillary" or "accessory" activities, that the whole purpose of the regulatory and supervisory system appears meaningful.

In the formal sense of the word a bank or an insurance company cannot be a broker for each other.

Art. 2 of the Investment Services Directive 93/22 shows that insurance companies cannot broke banking and investment products for others, and the definition of an insurance broker in Directive 77/92 seems to indicate that a bank cannot have the independence required from an insurance broker. If they want to deliver such professional services to their clients they must acquire an affiliate company with this social object.

When an bank or an insurance company distribute the products of each other they probably have the status of an agent under the general law of agency. It is hereby recalled that a variety of rules on contract, consumer and prudential protection require them to enclose the name of the bank or insurance company whose products they offer.

It should be added that Denmark has no legislation on insurance brokers. A legislation is, however, under preparation.

5.2. Contract and Consumer Protection Law Restrictions?

Introducing this subject it is important to describe the sources of law.

The starting point are the general rules of contract law. Especially important is the Contracts Act of 1917.

For insurance, this is supplemented by the Insurance Contracts Act 1930, and by the complicated private international law rules of the 2nd generation insurance directives.

The continental system of approval of general and special policy conditions never was much used. It was known in fire insurance where it is now taken over by a general regulation. In certain other cases policy conditions may be agreed between groups of insurers and policyholders, e.g. organisations of consumers or industry.

Besides, a good amount of commercial standards are being developed in practise under and besides the Insurance Contracts Act.

Finally there is the Fair Marketing Act, and the consumer and fair marketing protection enforced thereunder by the office of the Consumer Ombudsman. The role of the Ombudsman in later years has been great. The behaviour of insurance companies in the 80'ties gave rise to a number of interventions. But during this decade the behaviour of banks has qualified them as one of the most important hunting grounds of the Consumer Ombudsman in the quest for fair practises.

The Consumer Ombudsman is also the competent authority under the Payments Cards Act.

It is *per se* not illegal to market combined products that combine products of banks and insurance.

But it follows from an number of legal rules that the parts must be separable, so that the producers know for which parts each of them must build regulatory own capital, and that the client knows whom he has eventually to sue, as Danish agency law would not normally permit him to sue the agent for fulfilment of the contract, cf. also 9 *infra*.

A special problem for the consumer protection was that for many years banks tended to sell "combined" products for pension and retirement which contained either no or an insufficient risk coverage (which due to the actuarial element they could not produce themselves), but the clients were not sufficiently informed about the future consequences of such absence. Even though the authorities for many years tried to correct this, it is probably correct to state that it was rather the many alliances during the 1990'ties than law abidance that brought this to an end.

There are no specific rules for combined bank-insurance products. And it is doubtful whether it is possible or desirable to introduce such ones. In a rapidly changing environment it appears much better to leave this to the Consumer Ombudsman.

For many years the Insurance Act had a rule

requiring insurance products to be marketed by qualified persons. This rule gave great problems during the first years of bank-insurance, because it ended up as just an (*in*efficient) tool for the organisations of insurance employees resisting change, and was then abolished. Part of the problems behind it was and is that the insurance industry has organised a more centralised and better training than the banking industry through the Insurance High School, owned by the whole industry. However, in later years the banks have acknowledged this and sent massive quantities of their personnel to the Insurance High School.

Behind this is another question that is very much in the air in these years: What is the responsibility of liberal professions, including the financial ones, for negligence, including anonymous errors (not attributable to any concrete employee)? Should the onus of the proof be inverted and put on the financial enterprises? And should there be a contractual liability also for the client's reasonable expectations? When parliament some years ago permitted banks and insurance companies to act as estate brokers, it also introduced such a stricter liability – and to say that the financial industry loathe the prospect of this liability being generalised would rather be an understatement. But most likely, some legislation to this extend will be enacted during 1999.

It should be added that except for special cases as fire insurance for real estate, Danish law does not recognise the principle that everybody has the right to be served by banks and insurance companies, and even less that everybody has the right to contract the whole product range of bank-insurance. Thus the Payment Cards Act does not give everyone the right to get a payments card issued.

6. Company Law

6.1. General Observations

Several times we have illuded to the importance of general company law. This is true for several reasons.

First, unless for specific reasons the Banking or Insurance Acts apply, the Company Act applies. An example of this for financial groups was mentioned 3.2. on the social object of the mother company as a limitation to the activities in affiliated companies. Another example mentioned several times is the rules on shareholders loans, discussed *infra* 6.2.

The other reason is that the major part of the theoretical apparatus comes from company law. A glance at the recently appeared commentaries to the Danish Banking and Insurance Acts will illustrate the importance of general company law.

The scandals of bad management in some major Danish companies in the early 90'ties (the two biggest insurance groups, the second biggest maritime shipping and trading company, and one of the worlds leading feather manufacturers) led to considerations on whether this called for legislative action. The result was in the affirmative, but the actions were taken at the level of the Public Companies Act. It led to a major strengthening of the chapter on the duties of the board and the directors. These rules will strengthen the case of unsatisfied shareholders and creditors suing directors or board members for liability for negligence (in contract).

One important new rule, clearly inspired from financial supervision, but is applicable to all public companies , is now found in s. 54(3) of the Public Companies Act. It requires the board to see to it that the company/group always has a working capital that is adequate to the activities of the company/group.

6.2. Loans to Shareholders

In the early 1950'ties the Danish rules on "loans to shareholders" were introduced in the Companies Act.

Basically, the rules forbid such companies to give loans to shareholders. Such loans are seen as illegal distribution of dividends or as an informal reduction of the capital through the back door. It may also be contrary to the general principle of equality of shareholders when it is used by the controlling *clique*, and this is in itself a protection for minorities in affiliated companies. In the last decades, the rules have played a major role in stopping people from buying a company without investing; the law forbids them to buy the shares of a company and then pay the seller by means of money they "borrow" in the acquired company.

It requires no deep insight into psychology to realise that the life insurance funds present a great temptation to the group management in financial groups. This is especially true in two situations where there is a need for cheap money: When they want to expand quickly and greatly, and when they are in troubles, including a threat of "interest rate strangling". Here the management encounters the prohibitions of the Public Companies Act, reinforced by ss. 142 - 144 of the Insurance Acts which requires that even such transactions that are permissible under the Company Act are approved in advance by the Financial Supervision Authority.

6.3. Group Law (Konzernrecht)

An important part of the Company Act, both as regulation and as a service, are the rules on groups of companies (*koncern*).

Danish law does not have a systematic regulation like the Title III of the German *Aktiengesetz*. But added together, the law has a mass of rules for groups. Thus ss. 55 and 55a of the Public Companies Act create a constant duty of reciprocal information between the boards of the daughter and the mother company. But basically each company is an independent legal entity.

On a number of petty points, the Banking and Insurance Acts add regulation on intra-group relations, especially between directors and board members.

A rule of importance to groups with minorities in the daughters is s. 80 of the Public Companies Act, the so-called Nordic general clause. Under this the general assembly cannot adopt decisions which "evidently" are of a nature that may provide certain shareholders or others undue advantages at the cost of other shareholders or the company. The jurisprudence underlines that s. 80 primarily applies in intra-group relations.

It goes without saying that Danish law on capital adequacy and group accounting fully applies the various rules of EU law. But in many cases, Danish law completes EU law on the basis of our longer experience.

A special problem in financial groups is the eventual responsibility of the mother or all group members for the debts of a subsidiary company, be it to the creditors or to the minority shareholders.

Such responsibility (*Haftungsdurchgriff)* can, of course not normally be assumed between companies with limited liability, and requires a special basis which can be a contractual duty or a contractual or extra-contractual liability. The precise conditions under which such liability can materialise, is basically a judicial question, but the organisations of industry never wanted to try to fix some principles, and the area is therefore left unregulated.

This gives rise to special worries for the financial supervisor. It may be possible that this reduces the value of certain assets or creates a passive, not adequately covered by own capital. This is especially the problem when such liability is being decided in for-

eign courts of law or arbitration outside Denmark where the law applicable to a contract may not be the Danish law, and where the law on groupwise liability may be stricter.

The Danish supervisors should have a second worry. When a group presents itself as a whole with one trade mark etc., "it" may have to pay for the wrongdoings of one member without considering the likely outcome of a court case because the group's "good name" cannot support the publicity etc. This creates a contagion problem that is nearly an *insolubilium*. Such things require the caring eye of the supervisor for the group accounting, and for the correct calculation and (prudent) investment of the technical reserves in life assurance.

6.4. Special Problems for Mutuals and Trusts

When it came to building financial conglomerates or "supermarkets", the mutual insurers, the pension funds, and the saving banks found themselves at a disadvantage *vis a vis* the banks and insurance companies that were (public) joint-stock companies. They could not do the most desired thing: mutate themselves into affiliates wholly owned by a mother company, just created by themselves.

This led to an enormous creativity on the part of some insurance and mortgage bank boards and directors and their legal advisors. Associations transformed themselves into companies, or transferred part of the activities to companies which in their turn created their own mother. But the constructions remained somewhat imperfect, and had certain drawbacks: They required under association law often unanimity or a very qualified majority, they created tax law problems, and the costs were from a Danish vantage point quite exorbitant.

The saving banks had even bigger problems. As trusts (self-owning foundations) they were basically non-profit (albeit this was somewhat theory), but in case of transformation into another form of legal person the whole net own capital would be retained in the trust for good purposes *(pia causa)*, and/or submitted to liquidation taxation. This lead to amendments of the Banking Act to permit the change of form. It was, however, bitterly opposed by some members of parliament.

For pension funds, however, this does not apply. The law requires them to stay pension funds in the form of associations (co-operatives). In certain cases this has led the founders of the pension fund (Employers and Trade unions) to found an insurance joint-stock company to cater for future members.

Generally, these phenomena have created a tendency to use more or less solely the legal form of (public) joint-stock company. As it is the best regulated, tested and known this is in many ways to be greeted. And the Mortgage Banks Act requires future mortgage credit banks to be public companies.

Some feel, however, that this has made the financial world poorer, especially in the motherland of the agricultural co-operative movement.

7. Bankruptcy Law and Clients' Guarantee Schemes

7.1. Conflicts of Law

It is hard to judge the bank-insurance without looking briefly on the rules on the situation which basically all prudential regulation is set up to avoid: insolvent dissolution, normally in the form of bankruptcy.

First we must observe that in the EU area the biggest hole in the regulation is that neither is the bankruptcy convention in force, nor are the special directives on insurance and banks liquidation experience such as BCCI has demonstrated that cross-frontier insolvencies are virtually impossible to handle justly and efficiently without some harmonisation of

material norms and competence rules. As more and more financial groups have international links, we can establish a major systemic hole here.

As examples we can mention, that the rules on compensation and the bankruptcy estate's possibilities of "cherry-picking" of contracts differ. A bank-insurance group gives special problems because there will always be specific bankruptcy rules around life insurance contracts, and they will likely vary under the laws applicable.

7.2. Clients' Guarantee Schemes

In banking, there has been a tendency to remove some of the problems by obligatory guaranty schemes for deposits or investors. This tendency has been crowned in the EU by the Directives 94/19 and 97/9.

The Danish act specifically prescribes that pension schemes in Danish banks are to be paid out in full and without possibilities of compensation.

However, the Danish banking deposit guarantee scheme may, since 1996, also assist in the reconstruction of banks. (This possibility has increased in importance after the EU Commission began to enforce the state aid rules, see 8.2.).

It should be mentioned that under the Fair Marketing Act, the Consumer Ombudsman has prohibited banks from marketing their products as especially safe due to the fact that deposits are protected under the deposit guarantee scheme.

In mortgage credit, the same problems should in principle exist. But as mortgage banks are specialised institutions under a strict balance principle, problems can only arise in case of criminal activities on a major scale.

In insurance, policy holder protection schemes are a natural correlate of obligatory non-life insurance (cars, dogs, nuclear damage, works accidents). It is also prescribed for the quasi-obligatory fire accident insurance for real estate where it applies to established business and service business alike.

There are no schemes in life insurance, but here the Supervisor has the possibilities of taking under administration all assets registered for covering the technical provisions calculated by the actuaries of the supervisory authority. The administration scheme has never been applied in practise, but the threat is very useful and potent in case of financial conglomerates.

In the beginning of the 80'ties a committee considered the possibilities of schemes like the fire insurance scheme for all insurance. The idea was shelved because it proved to be technically very difficult and out of proportion to the problems likely to arise. The experience since then has affirmed this. But at the same time the tax law has thinned out the reserves of life insurance, see 12 *infra*.

8. Supervision

8.1. The Organisation of Supervision

During the 1980'ties all supervisory authorities were merged into one. The main motive was modernisation and effectivisation of the state apparatus. Therefore everything relating to company law and shareholder protection is in the Companies Register, all competition questions with the Competition Agency, and all consumer protection questions are with the Consumer Agency and the Consumer Ombudsman even though certain actuarial questions and securities trading questions would in practise often be solved by the Financial Supervision Authority.

But when merging, also considerations on the then rather new financial conglomerates had some importance. With hindsight it must, however, be stated that the merger was technically and personwise more difficult to manage than foreseen, and that the so-called synergy effect took some years to materialise.

8.2. Special Rules For Conglomerates

It is appropriate to begin by one very practical precision to the role on supervision in relation to the "activity" of a conglomerate.

The introductory words of art. 57(1) of the EC Treaty introduce the distinction between "access" and "exercise" of an activity. The home office rule basically only applies to access. The activity/exercise is basically regulated by host country law, at any rate in so far as contract, marketing, consumer protection law, and insurance contract taxes are concerned. This has now been established more clearly by the *Keck* decision of the Court of Justice (1993).

This is the core of the intention behind the competence distribution in art. 21 of the 2nd banking directive, and art 40 of the 3rd generation insurance directives. And to countries like Denmark with a highly developed consumer legislation it is of utmost importance. Whoever is the competent authority under the home office principle, Danish consumer protection law applies in Denmark.

It should be added that this corresponds to the general principles of private international law as embodied e.g. in the EU's Rome convention (1981).

A special license for conglomerates appears not possible under the EU directives. The only possibilities for the supervisors is to stop such conglomerates that are intransparent, or are controlled by unfit or unproper (destructive) shareholders. After all, enterprises have the right to organise themselves in the way most desirable to themselves, and unless there are important, concrete reasons this is not a matter for public authorities.

Financial conglomerates cause important but highly complicated additions to the capital adequacy rules, and rules on consolidated accounts and supervision.

The consolidated supervision must, however, differ between banks and insurance. For bank-dominated conglomerates consolidation is the best starting point. For insurance the starting point for a number of technical reasons (e.g. reinsurance, actuarial) is the opposite, (sometimes called "solo plus"), and this must apply even at group level, i.a. because of reinsurance and actuarial considerations.

The later years have taken away from EU supervisors one weapon of discreet rescue: financial state support. It is now firmly established that this constitutes state aid, and the publicity and delays prescribed under article 93 of the EC Treaty removes much of the attraction of this avenue.

8.3. The Civil Responsibility of Supervisors

It is also appropriate to mention the civil responsibility of the Danish supervisors.

Like all other civil responsibility it is based on case law. The courts apply the same standards to public authorities as to all others, but of course the requirements for a *bonus pater* supervisor are relatively strict. There are no cases for the financial supervisors (but one major case in the pipe line). But two land mark cases are of interest to financial supervisors. One ordered the state to pay compensation because the police did not alert the fire brigade very quickly. The other held the police responsible to the buyer of a car for hidden errors which could and should have been detected during the technical control of cars.

This being said it is urgent to underline that the Banking and Insurance Acts do not issue a guarantee that financial companies, and even less conglomerates and groups, are solvent. The Financial Supervision Authority does no more "guarantee" the solvency of supervised companies than the road police "guarantees" that all drivers respect the speed limits.

In relation to the home office principle of EU law this gives the clients/consumers a

problem: What is the responsibility of the foreign supervisor of a branch office situated in Denmark. Probably it is less strict as is the case in our closest neighbours, Germany and Sweden.

8.4. International Co-operation

As an EU member, Denmark is of course participating in all committees of the Council and the Commission, including the Banking Advisory Committee (BAC) and the Insurance Committee (IC). We also participate in the Conference of Insurance supervisors, the Banking Contact Committee, and some bodies under the ECB system. Generally, it can be said that due to the relatively advanced stage of Danish law, Denmark has been a very active player in these fora on bank-insurance problems.

Equally, we of course participate in the world wide fora: IAIS and IOSCO. The BIS is more exclusive and has not taken in all member states. But it should be noted that the relations between these bodies and the EU are not correct under the doctrine stemming from the Court of Justice's AETR-doctrine, because the Commission does not represent the EU.

Many years of co-operation of course forger close links between supervisors and their personal. But the home office principle also creates practical links under which supervisors take actions originating from a brother authority in another member state. Furthermore, the home office principle causes supervisors to inspect *sur lieu* in other member states, and this of course creates new links.

The more formal liaising in the form of memorandums of understanding has revealed itself to be a cumbersome procedure. Denmark has not found it especially attractive or required. (Either we are too small, or our supervisors are too good, but so far the international conspiracies have not unduly burdened the Danish system.)

9. Dispute Settlement for Consumers

Part of the Danish consumer protection legislation is the Consumers Complaints Tribunal Act where consumers can obtain a cheap and speedier conflict solution.

The Act allows the Consumers Complaints Tribunal to permit that, upon agreement between consumers organisations and organisations of a specific sector, a special complaint tribunal be created for that sectors.

Both for banking and insurance, such tribunals have been set up. In cases of combined products, the case will have to be split up and presented to both tribunals.

The tribunals are financed by the sector in question. The members are representatives from the sector and the consumers, and the chairman is normally a supreme court judge.

There can be discerned – in comparison to the ordinary courts – a tendency to use *ex aequo et bono* elements in the tribunals' decisions.

The tribunals must be characterised as quite successful both by permitting "to let the steam out" and keeping banks and insurers up to standards, but also by their contributions to a constantly modernising of the norms for good banks and insurance companies, cf. 5.2 *supra*. Only few of their decisions are not respected and/or sent on to the ordinary courts.

In case of disrespect, the public Consumer Ombudsman may take over the case under the Fair Marketing Act.

10. Competition and Cartel Law

10.1. General Rules of Danish Competition Law

Financial companies in Denmark are submitted to both the Danish Competition Act and the EU rules.

In 1997, Denmark got a new Competition

Act. This act “copies” the EU rules, except that it has no merger control.

An interesting feature is that the act expressly declares itself secondary in application to part of the EU law. This *renvoi* applies to “agreements, decisions, and concerted practises which have received an exemption pursuant to the EC Treaty, or which fulfil the conditions in a regulation on block exemptions”. These are outside the scope of the Danish act.

Thus, it can be said that the Danish financial sector is basically under (only) such material norms on competition as we know from EU law (except for the absence of local merger control).

10.2. Specific Cartel Rules for the Financial Sector

Because of short time since the entry into force of the new act, it is too early to predict what special rules, if any, there may be for the financial sector. And there is little practise under the earlier laws that can be transposed to the present day situation.

However, it is not likely that the new act will impose undue restrictions upon the freedom reigning today. There appears no reasons for specific restrictions. And supposedly the organisations of banks and insurers will themselves apply a self-discipline and thus avoid conflicts.

It should be mentioned that due to the EU *renvoi* principles described in 10.1, there was issued a Danish regulation exactly corresponding to the EU regulation 3292/92 on certain permissible agreements between insurers.

11. Data Protection Law

11.1. Registration of Data

Under Danish law, the data protection of banks and insurers is governed by the Private Register Act of 1978.

According to section 3 of the Private Register Act, *registration* of absolutely private data is permitted if concerning the interest of the registering party or other *and* the information is either submitted by the person being registered or obtained with his consent, whereas registration of other data as an ordinary part of the registering party’s business does not require any consent.

The legal exemplification of the omnibus clause ”absolutely private data” includes race, religion and colour, political or sexual status, punishable offences and information on health, essential social problems and abuse of narcotics.

Thus, insurers may only collect data on the health of persons insured directly from the insured themselves, or with the consent of the insured. The data obtained may only be divulged to third parties, e.g. other insurers, independent medical advisers or the courts, with the explicit consent of the insured.

Private registers containing absolutely private data must be notified to the registration authorities. Inspections as to the content of the registers are carried out on a regular basis, ensuring that the law (incl. supplementary internal instructions) is being abided by.

Finally, data that has become obsolescent must be deleted.

11.2. Use of Registered Data

It is legal as an ordinary part of the registering party’s business to pass on data except the absolutely private data without the consent of the person concerned. As a result, banks and insurers are able to and do exchange information on certain groups of customers, e.g. for marketing purposes.

It is illegal, however, to exchange any kind of specific data on customers if done for the purpose of warning against certain customers – unless such an exchange of data has been specifically authorised by the authorities. This

is by definition a problem to all financial groups, as it has always been a problem and a barrier to insurance groups which by law have to consist of a life and a non-life company.

Such authorisation has been sought and obtained by both the Danish banks, having established a joint register of check abusers, and by the Danish insurers, having established a joint register of high-risk customers.

11.3. Securities Market Regulation

The Securities Trade Act 1995 contains rules restriction the storage and use of internal knowledge. This is done in conformity with the Insider Directive (89/592).

12. Tax Law

12.1. The Importance of Tax Law

It appears from a Danish point of view difficult to meaningfully discuss financial groups' problems without including some words about tax law.

Here we can just list some examples. But it is recalled that in a country like Denmark where the taxman takes more than half of the GNP, tax policy is often markedly short term oriented. There have been three "major tax law reforms" within the last dozen years.

12.2. Company taxation

The very existence of a group may depend upon the possibilities of being taxed as one economic unit. This is possible in Denmark.

The VAT legislation also rewards those groups which have an intra-group company for information services, because those many companies which would use an external computer centre are fully submitted to the VAT.

A related phenomena is the so-called "outland easement" for operations in other countries. It applies to all industries with activities outside Denmark. It is pendulum-wise tightened or loosened as part of the overall tax policy. And as the bigger financial enterprises have more and more activities, be it core business or ancillary activities, outside Denmark this is of some – and unforeseeable – consequence.

During the last 10-15 years the tax law has thinned out the reserves of life insurance, due to two things. First, the possibilities of transferring untaxed profits to a "safety fund" for future bad luck has been abolished. Second, there is a special tax on the income from the assets of life insurance (p.t. 26%).

12.3. Personal Taxation

With a progressive incomes tax scale that reaches 62 per cent, and easily, even for the middle class, gives a effective tax rate of more than 50 per cent, pension savings must either be enforced (which they to a great extend are through the labour market agreements) and/ or deductible in taxable income. The latter is also being done, albeit reduced somewhat in value during the later years.

This reduction applies especially to such non-risk "capital pension" products which banks can subscribe. As mentioned under 2.1 the bitter fight in Denmark for pension savings began in the 70'ties because tax law amendments, under pressure from the banks, gave "level playing field" to banks and insurance in the area. The banks thereby greatly increased their long term deposits. This made perhaps at the time political sense, but was to some extend technically meaningless, and it had an adverse long term effect. It triggered off years of futile marketing wars on who would perform better in 30 years time, in which war the consumers were not always the winners. And an increased part of non-risk pension savings from a state budget point of view tampered the national economy by burdening the social pensions system unduly. As

the deduction premium on non-risk “capital pension” products is being reduced, the pendulum may swing back in favour of life insurance.

13. Notes

[1] The manuscript was originally prepared for V. AIDA seminar on insurance law in Budapest 26 – 28 November 1998.

[2] IAIS = International Association of Insurance Supervisors; IOSCO = International Organisation of Securities Commissions; BIS = Bank of International Settlement.

[3] One major contribution to the literature in the field was the *XV. FIDE Congress (Lisbon, 1992), vol. I & vol: Conclusions des traveaux: ”Les prestations des services financiers au sein de la CEE et avec les pays tiers”*. I submit that my general report, together with the conclusions and the questionnaires on which I based it, still constitute one of the most comprehensive treatment of the subject.