

**STRUCTURE OF THE RUSSIAN INSURANCE MARKET AND EXPECTATIONS
OF ITS DEVELOPMENT**

**By the Ministry of Finance of the Russian Federation
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1245 insurance companies were registered in Russia as of October 1, 2000. For the past two years the number of insurance companies decreased by more than 1000. This was mainly due to the reinforcement of the control by the insurance supervisory authority for the observance of the requirements of the Russian insurance legislation and to the fierce competition between the insurers resulting in the cessation of activities by many small and medium companies.

The aggregate chartered capital of insurance companies reached 12.4 billion rubles, i.e. more than 444 million USD.

Before the year 2000, according to the requirements set by the Law, the paid up chartered capital of companies registered earlier should have been raised up: 75.000 USD for the companies carrying on non-life insurance, 105.000 USD for life insurance companies and 105,000 USD for reinsurers.

57 new insurance companies were registered during 1999 and 50 companies within the first 9 months of 2000. The licenses of 800 insurers were suspended or withdrawn for various violations of the law. About 700 insurance brokers are registered with the Ministry of Finance. The Russian legislation does not prevent foreign insurance brokers from establishing their affiliates and offices in the territory of the Russian Federation. However, their activities are limited by allocation of insurance risks to the Russian insurers only.

60 companies with foreign participation are registered on the Russian market. The consolidated share of insurers with foreign participation in the total volume of insurance premiums collected during the first 9 months of 2000 was slightly more than 10.9 % in voluntary insurance and about 7.8 % in non-life insurance.

The number of professional reinsurers in Russia practically did not change during the last years and is equal to 23. The share of Russian reinsurers in the total volume of insurance premiums collected in voluntary insurance other than life insurance is about 5.4% and 1.9 % in payments made.

Development of insurance operations

The total volume of premiums collected by the Russian insurance companies for the first 9 month of 2000 is 118.5 billion rubles, which represents more than 1.7 times growth and corresponds to 4% of GNP.

The amount of insurance premiums per capita in the Russian Federation is 817 rubles or 29 USD.

Voluntary insurance developed rapidly: premiums collected in different lines of voluntary insurance increased by 1.8 times. The share of premiums in voluntary insurance continued to grow and reached 77.3 % of the total volume of insurance premiums collected during the first 9 months of 2000.

A serious reason restraining the development of property insurance in Russia is the limitation of this insurance to 3 percent of the prime cost of goods manufacturing, works and services. Therefore, the insurance of industrial enterprises is notably insufficient, leading to low rates on the insurance market and distorting the real demand in insurance protection. Amendments to the legislation envisaged in the draft of the second part of the Taxation Code should drastically influence the formation of solvent demand for property insurance and the liability insurance in industry, trade, agriculture and other sectors of the economy.

Increases in the rates and volume of insurance premiums are stemming from the strong growth of property insurance (the growth rate during the first 9 months of 2000 was 1,5 times greater than the rate for the corresponding period of the previous year), liability insurance became 1,8 times greater for the same period and life insurance doubled. As a result, the share of property insurance including the liability insurance in total insurance premiums collected by the Russian insurance market was 25%. The concentration in non-life insurance business is rather high. The 100 largest insurers collected 80.7% of the total volume of non-life insurance premiums.

Life insurance preserves its leading position on the insurance market. Its share is more than 48.6% of the total volume of premiums, doubling in the first 9 months of 2000. Insurance benefits in life insurance represent 55.7% of the premiums collected. Insurers managed to overcome negative tendencies caused by the economic crisis of 1998 which provoked sharp growth of pre-term cancellation of insurance contracts, leading to a dramatic growth in insurance payments (the level of insurance payments exceeded the premiums by 6 points in life insurance operations on the whole in the insurance market).

The main demand for life insurance remains determined by the interest of corporations in group life insurance for their employees. Market leaders offer insurance products that combine both insurance and saving elements taking into account the requirements of the insurance and taxation legislation in force, e.g. long-term annuities and other life insurance products for which both employees and employers pay contributions. For lack of legislative incentives, there is so far no market for long-term products in pension insurance. Nevertheless, this problem is one of the main concerns of the insurance community and is planned to be resolved through taxation law.

The concentration in the life insurance sector is much higher than in other insurance lines. The 100 largest insurers are collecting about 55% of premiums.

On the reinsurance market, national reinsurance companies are competing with the international brokers and reinsurers. For this reason, data related to the development of insurance operations of the professional Russian reinsurers, do not reflect the real scope of reinsurance activity. The share of cross border reinsurance operations is extremely high, taking into account the rather low capitalisation of the Russian insurance and reinsurance markets. Offices of the largest international reinsurance companies are registered in Russia.

Regional Aspects of the Russian Insurance Market Development

The insurers registered in Moscow have a decisive impact on the development of the Russian insurance market. Their share in total insurance premiums collected is more than 63%, although the number of Moscow-registered insurance companies is slightly more than one quarter of the total number of insurance companies. It is mainly to be explained by the fact that the largest Moscow insurance companies have a well-developed branch network (up to 60-70 branches working practically in all regions of the country). Besides, they use a wide network of insurance agents and representatives in the biggest cities and districts of Russia.

Such wide representation in all regions of the country allows them to increase the volume of insurance operations using modern technologies and to supply new insurance products.

Insurers of Tumen District, City of St-Petersburg, Samara District, Moscow District, Kemerovo District and some others are the important players in the Russian insurance market.

The role of the regional insurers is particularly great in compulsory medical insurance. Their share in this type of insurance is more than 70% of the total volume of insurance operations.

Expected Development of Insurance Market

The role of insurance in the Russian social and economic system should increase if the main economic parameters in the insurance market remain stable and if state regulation is both strengthened and extended.

It is expected that basis indexes of the Russian insurance market will increase in the middle term. The ratio total insurance premiums/GNP is expected to increase up to 5-7%.

The number of insurance companies should stabilise between 700 and 900. Relatively big interregional insurance companies are being established. Foreign capital market share will increase gradually up to 12-14%.

Long-term life insurance is being developed, including pension insurance as well as voluntary medical insurance and some other types of insurance, which become an important element of social protection.

A less important element of the Russian social and economic system is the mechanism of compulsory insurance. A number of new lines in industrial insurance are being introduced, especially in financial risks insurance.

These developments may eventually decrease the budget burden related to the necessity to overcome the consequences of catastrophes, natural disasters and other events causing substantial property damage, and to the necessity of social support for the population.

The practice of market regulation and control

In accordance with the Law of the Russian Federation "On organisation of insurance business in the Russian Federation", the regulation of the insurance market and control over its participants are placed under the responsibility of the Federal executive insurance supervisory authority and its regional inspections (at present, these functions are entrusted to the Ministry of Finance of the Russian Federation).

This insurance supervisory authority has the powers to set:

- order of licensing of insurers;
- conditions and principles of insurance and reinsurance;
- rate policy, size and structure of tariffs in compulsory branches of insurance;
- standards related to the solvency of insurers;
- requirement referring to constitution, investment and use of insurance provisions;
- maximum volume of insurance liabilities which the insurer leaves without reinsurance;
- rules and conditions of setting and submitting accountancy and statistics, procedures of disclosing information to the supervisory authority, instructions of reflecting the transactions in the accounts.

The federal executive insurance supervisory authority elaborates normative and methodological documents on insurance activity and standardises the practice of insurance activities. It submits proposals concerning the development and improvement of the insurance legislation of the Russian Federation and takes part in the elaboration of the Federal laws related to insurance.

In order to control insurance activities , the supervisory authority has the right to:

- exercise preliminary control by licensing insurance activities on the territory of the Russian Federation, by issuing preliminary approval to raise the authorised capital with the help of foreign investors and/or affiliates, and by controlling foreign investor's transactions related to the alienation of the shares in the authorised capital of insurance companies and on establishment of affiliates by insurance companies with foreign participation;
- analyse the financial soundness of insurers and establish the United State Register of Insurers and Insurance Brokers;
- control the validity of insurance tariffs, the insurance provisions, the investment of reserves and the analysis of the reports on insurance activity submitted by insurers;
- request the reports on insurance activities and on insurers' financial soundness, and obtain from enterprises, including banks, as well as from citizens, information related to insurance operations;
- assess the compliance with the requirements of the insurance legislation of the Russian Federation, and check the accuracy of the disclosed information by insurers;

- prepare documents necessary in order to liquidate the insurance company in case of repeated violations of the legislation by the insurer or in case of operation without a license;
- prepare materials in order to support a claim when an insurer has illegally capitalised reserves, with the aim of transferring these sums and the accrued interests for the State budget.

If the supervisory authorities reveal the violations committed by an insurer, they request from this insurer that he abides to the law. If the insurer fails to fulfil these instructions, the federal executive supervisory authority either suspends or limits its license or decides to revoke the license.

The relations between market players in the field of insurance are regulated by the normative acts of the Civil Code of the Russian Federation, the Law of the Russian Federation "On the organisation of insurance business in the Russian Federation", and by other regulative and legislative acts of the Russian Federation.

The insurer has the right to carry on insurance business after he has received a licence authorising him to perform insurance activities. The process of licensing insurance activities is defined in the legislative act entitled "the Conditions of licensing insurance activities in the territory of the Russian Federation".

Only legal entities may act as insurers (physical persons and individual entrepreneurs can not act as insurers), established in any organisational and legal form stipulated by the law of the Russian Federation to carry on insurance activities (insurance undertakings and mutual associations).

Industrial, commercial and banking activities may not be subject to direct activity of insurers.

Licenses are issued by the insurance supervisory authority to carry on voluntary and compulsory:

- personal insurance
- property insurance
- liability insurance
- reinsurance if the activities of the insurer is the reinsurance only.

Specific scopes of insurance activities in which the insurers have the right to operate are indicated in the Annex to the license.

In conformity with the Law, the insurance supervisory authority has the right to lay down requirements as regards the bookkeeping and the reports on insurance activities.

Special forms of accounting for the insurance companies are set in the Russian Federation (balance sheets and report on profits and losses) which are close to requirements of the European Community Directive related to the reporting on insurance undertakings.

Besides, a new special "Chart of Accounts for insurance undertakings" and Instruction on how it should be used have been approved. They are being presently revised in connection with the endorsement in October 2000, by the Ministry of Finance of the Russian Federation, of "the United Chart on Accountancy of Financial records" for all types of undertakings.

Insurance companies, alongside with the accounting statements, submit to the Ministry of Finance of the Russian Federation some special fixed-format reports for supervisory purposes (on solvency, allocation of reserves, use of the reserve for preventive measures and some others).

Presently, in the framework of the Programme of reforming the accountancy in accordance with the international standards of financial reporting, the original document, worked out by the Working Group of the Committee for International Standards of Financial Reporting, referring to elaboration of the standard "Accountancy of the insurance undertaking"; is being studied in order to prepare a standard for insurance companies and to harmonise the national system of book keeping for insurance undertakings with the international standards of accounting.

The legislation stipulates the powers of the Ministry of Finance to lay down the rules on the formation of technical provisions, on the investment of assets covering technical provisions, and on the requirements relative to the matching of assets and liabilities (solvency margin). The approach adopted by the regulators is close to that implemented in the EU member countries.

Some changes in the calculation of solvency margin are being planned to be introduced in order to take into account the volume of future claims (in non-life insurance) and the value of the capital at risk (in life insurance) with a view to comply to a greater extent with the EU Directives' requirements.

In accordance with the legislation of the Russian Federation, the assets matching the technical provisions must satisfy the requirements of diversification, profitability, refundability and liquidity.

"The Rules of Technical Provisions Investment" lay down the requirements for assets matching technical provisions. These requirements include: the composition of assets, qualitative characteristics of assets, limitations on the amount of assets (as compared to the amount of technical provisions) accepted as cover for technical provisions, for each type of asset and for each asset (for each debtor).

Currently the "Rules on the establishment of life insurance provisions" are worked out. They are planned to be introduced in 2001. According to these Rules, the calculation of provisions is based on actuarial methods.

The legislation does not enforce any restrictions on the investment of the part of assets representing the own equity of the insurers.

Organisation of Insurance Supervision

The Department of Insurance Supervision is a structural unit of the Ministry of Finance of the Russian Federation enforcing the implementation of the state supervision over insurance activities.

The basic tasks of the Department of Insurance Supervision are:

- carrying out within its competence the state supervision over insurance activities in the Russian Federation with the view to ensure observance of the Russian Federation insurance legislation requirements, effective development of insurance services, protection of rights and interests of insured, insurers, other market players and the state;
- ensuring, in accordance with the approved order, the licensing of insurance companies;
- ensuring methodological management of accounting and statistical reporting of the insurers;
- co-operating with the international organisations in the field of insurance regulation and supervision.

The Department is headed by the Director who is appointed and dismissed by the Minister of Finance of the Russian Federation. The regional inspections that perform their functions in compliance with the Department of Insurance Supervision are now being reorganised taking into account the Structure of Federal Divisions.

Insurance Market Liberalisation

At present, Russia is undergoing a process of integration into the world financial market. Increasing co-operation with the international financial institutes and strengthening and developing mutually beneficial economic ties are the priorities for the further development of the Russian economy as a whole and of insurance market in particular.

National insurance market development is also measured through the degree of liberalisation of the access to the Russian insurance market for the foreign insurance companies.

On the 20th of November 1999, a new Federal Law "On Introduction of Changes and Amendments to the Law of Russian Federation "On Organisation of Insurance Business in the Russian Federation"" was adopted, which determines the terms and conditions of foreign insurers operation on the Russian market.

The regime of access, relating to the foreign capital participation in Russian insurance undertakings, is applicable only towards those insurance companies which have more than 49% of foreign capital share, but which do not exist due to the requirements of the Resolution of the Supreme Soviet of the Russian Federation "On the introduction of the Law on insurance in the Russian Federation". Besides, these limitations are not applicable to the activities of the insurance companies which were established before the adoption of the new law and which have less than 49% of non-resident share in the chapter capital. The adopted measures are oriented, first of all, to ensure the access to the insurance market of reliable and experienced foreign companies; to minimise insurance fraud cases and to protect the rights of the insured.

The limitations on underwriting certain types of insurance by insurers with foreign capital participation are, firstly, in agreement with the paragraph 3B of the Amendment 7 "Financial Services", according to which Russia may introduce limitation measures for issuing licenses to EU companies in the field of compulsory insurance, social insurance and state deliveries. Secondly, these limitations will allow to preserve the investment potential of the national insurance market and to prevent from currency provisions flowing abroad.

The special requirements applied to senior management are established with a view to guarantee civil rights and freedoms of the residents and to enhance the observance of insurance contract law by insurers in the absence of harmonisation of many items relating to the law, in particular in the field of struggle against insurance crime.

The above mentioned law was meant to improve the Russian insurance legislation and strengthen the control over activities of insurance companies on the territory of the Russian Federation accordingly to the EU practice.

The regime introduced is temporary and is aimed at using the insurers' investment capacities in the interests of the Russian economic development in order to create a system of insurance protection and to reinforce international co-operation.

Similar measures have been introduced in a number of countries: USA, Japan, Czech Republic and others.

At present, the Russian Federation participates in negotiations with a view to join the World Trade Organisation. The General Agreement on Trade of Services (GATS) that provides a basic rule for the application of the most favoured nation clause, allows the exemptions from these rules for a transition period of 10 years.

Taking into consideration the real situation on the national insurance market as well as strengthening protectionism tendencies in the world, the position of Russia, directed towards gradual liberalisation of the national insurance market and reflected in WTO special commitments, appears to be justified.

As a result of consultations with the domestic insurance community and with the leading insurance countries held in Russia in 1999 and in the first half of 2000, the process of liberalisation of the access to the Russian insurance market emerges to be the following:

- Adoption of the Federal Law on Insurance Supervision, which would strengthen the regulation of the market and would bring new dimensions and quality to the state regulation;
- Introduction of a system of control over insurance companies solvency;
- Application of the international standards on accountancy in insurance;
- Adoption of taxation schemes which take into account the specificity of insurance.

If these principal measures are to be realised in the coming years, the access to the Russian market would be compatible with those which now exist in the developed countries.

The liberalisation of the national market and its future integration into the world market is a historically non-alternative process.