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Liberalization of the Russian Insurance Market in Light of Russia's Accession to the World Trade Organization

MACD Project

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Scenario

This Project was completed as part of the requirements for the program of Master of Arts in Commercial Diplomacy at the Monterey Institute of International Studies.

For the purpose of this project, I will assume the role of an independent consultant to the Ministry of Economic Development and Trade of the Russian Federation. In light of Russia's ongoing insurance reform and efforts to gain access into the World Trade Organization (WTO), the Minister appointed me to develop a comprehensive strategy for reforming the regulation on the sale of mandatory insurance by foreign insurers.

Acronyms

AIG	American International Group
ARIA	All-Russian Insurance Association
CIS	Commonwealth of Independent States
CSR	Center for Strategic Research
GDP	Gross Domestic Product
ISD	Insurance supervision department of the Ministry of Finance of the Russian Federation
OECD	Organization for Economic Cooperation and Development
RUIE	Russian Union of Industrialists and Entrepreneurs
SRB	Self Regulating Body
WTO	World Trade Organization

EXECUTIVE SUMMARY

ISSUE

The Russian Federal Law on Insurance (1999) prohibits the sale of life and mandatory/compulsory types of insurance by majority foreign owned (>49%) insurers. Foreign participants in the insurance sector are unsatisfied with the level of protection for domestic companies. According to the Law, foreign insurers cannot make investments that would provide control over their Russian subsidiaries without losing mandatory and life insurance licenses. This issue inhibits Russia's WTO accession process.

RECOMMENDATION

It is recommended that the Ministry of Economic Development and Trade of the Russian Federation initiates a reformulation of Russia's WTO accession negotiating position with the view of allowing foreign companies' access to the domestic non-state mandatory insurance market.

Such a reformulation, conducted in accordance with the proposed strategy, will help the Russian negotiating team move forward accession talks with their WTO counterparts, while advancing the much needed modernization of insurance related policies and domestic legislation.

The recommended timeframe for the implementation of the proposed strategy is 2002 through the first half of 2003. At the end of this period, Russian Federation legislation on mandatory automobile owners liability insurance takes effect. This legislation alone will expand the Russian insurance market by \$1 billion. The ability of foreign investors to participate in such a large sector of the insurance market guarantees their active support for this proposal and guarantees more effective transfer of new technologies.

Benefits to the National Economy

Foreign companies' access to the Russian insurance market benefits the national economy in the following ways:

- Inflow of additional capital to the insurance sector;
- Transfer of advanced technology, experience, and education; and
- Introduction of price competition.

The widely held belief that foreign companies' access to the Russian insurance market will significantly increase outflow of the capital is disproved by examples in other transition economies. The protection of the domestic insurance market

does not solve the problem of capital outflow from the country. Domestic insurance companies equally contribute to the capital outflow through reinsurance and placement of investments abroad. Further elaboration of legislation regulating placement of capital and reinsurance abroad is necessary to address the issue of capital outflow.

PROPOSED STRATEGY

In order to reformulate the WTO accession negotiating position on insurance and to amend existing discriminatory insurance legislation it is recommended that the Ministry builds a coalition that includes the following: the All-Russian Insurance Association (ARIA), the Russian Union of Industrialists and Entrepreneurs (RUIE), the Ministry of Finance, the Prime Minister, and the President.

The Ministry's support for ARIA's strive to become an independent self-regulatory body as well as the explicit intent of the proposed reforms to streamline the insurance regulation will guarantee ARIA's cooperation. With respect to the matter of the proposed reform RUIE's membership is interested in speedier accession to the WTO and in being able to bring their own captive insurance companies to the foreign markets. Considering the relationship between ARIA and RUIE, ARIA's support for reform support of RUIE. The business community's backing for this proposal facilitates the further strengthening of the coalition by engaging the Prime Minister and the President.

A coalition built along the lines described above will make possible the implementation of the LEGISLATIVE STRATEGY, that will secure foreign access to the Russian non-state mandatory insurance market. The strategy will ensure passage through the Federal Assembly of sufficient combination of insurance legislations: a) Law on Insurance; b) Law on Insurance Supervision and Regulation; and c) Law on Mandatory Insurance.

Issue

The Russian Federal Law on Insurance (1999) prohibits the sale of life and mandatory types of insurance by the majority foreign owned (>49%) insurers. Citizens of Russia are obligated by law to insure certain types of risks, mostly third party liability. If the law stipulates that an owner or an operator must insure an asset or the liability that might arise from operating this asset, then this type of insurance is called *mandatory (or compulsory) insurance*. Currently, mandatory insurance represents 14.6% (or 40.3 billion rubles, 2001¹) of the total insurance market². Foreign participants in the insurance sector are unsatisfied with the level of protection for domestic companies and their inability to acquire licenses for sale of mandatory insurance.³

The mandatory insurance sector is poised to expand after the upcoming adoption of legislation on mandatory insurance. Foreign insurers invest in the established leaders of the Russian insurance market. Prohibition on the sale of mandatory insurance limits foreign companies' ability to make additional investments that would secure their control over their subsidiaries.

Mandatory insurance in the mind of many Russian legislators, government officials, as well as the general public, includes mandatory insurance for government needs; such as military and police force casualty insurance, state property insurance. Mandatory insurance also includes compulsory insurance to be paid by private citizens and corporations like automobile owners, auditors liability, liability from running high risk operations.

This project addresses only the latter part of mandatory insurance: collected from the private citizens and businesses. This project excludes the consideration of mandatory government insurance for the following reasons:

– Such insurance represents part of the social security system of the Russian state, and therefore performs the function slightly different than traditional insurance. For example, social security represents pensions paid to the families of deceased military or police personnel.

¹ All-Russian Union of Insurers, Bulletin of the Committee for Foreign Affairs #3 2001, p.8

² Another insurance sector closed to the foreign insurers is life insurance. Markets for mandatory and life insurance develop differently. Life insurance market is qualitatively different from mandatory insurance in the way that life insurance is related to accumulation of long-term capital and is more pronged to perform savings function. For purposes of this project we will focus of access of foreigners only to the mandatory insurance market. This figure includes premiums collected for mandatory health insurance. At present there is a tendency to separate healthcare insurance from the rest of mandatory insurance. As economic and commercial analysis will show, presently, purely mandatory insurance accounts for roughly 1% of the market, however it is poised to expand with adoption of new legislation.

³ List of national barriers to trade 2001

- Government insurance is paid out of the state budget (either federal, state or local level). Foreign companies access to this market is highly unlikely in Russia in the foreseeable future, since it would require the participation of the Russian Federation in the Government Procurement Agreement in some form.

Soviet Insurance Industry

There are two survivors of the Soviet era insurance sector: Ingosstrakh (International State Insurance) and Rosgosstrakh (Russian State Insurance). Over the years of economic reforms both of these enterprises have been privatized to different degrees. Due to the privatization that started in 1991 initial capital of the Ingosstrakh was diluted by 650%. Later, ownership of Ingosstrakh transferred from different industrial groups to a single majority owner Avtobank.⁴ However, in late October of 2001 the companies of Nafta-Moscow, Millhouse Capital and SibAl formed an alliance to purchase Ingosstrakh.⁵ The new alliance is closely related to the Russian Aluminum Consortium.

Ingosstrakh has a widely recognized brand in the foreign markets. Ingosstrakh received the golden prize “Brand of the Year/EFFIE-2001” in the nomination “Insurance”.⁶ Ingosstrakh has more than 50 years of international market experience. Before the reform, the company’s only drawback was limited to insufficient experience in working in the consumer sector. However, now the company is one of the leaders in all insurance sectors.

Due to numerous dilutions of company’s capital and government’s inability to purchase new stock in the company, the Russian State’s share in Ingosstrakh has decreased to 2.55% in 2001⁷.

The future of the company’s ownership is indeterminate at this point in time. However, there are speculations that the final recipient of the company’s stock will be AIG.⁸ AIG needs the investment in Ingosstrakh to be able to compete with its long-time rival in the Russian market German Allianz AG.

Fate of Rosgosstrakh is quite different. The company has not been privatized since the beginning of reform. It was only in 2001 that the Russian Government decided to sell 50% minus 1 share of Rosgosstrakh. The Investment Company “Troika Dialog” purchased 9% of Rosgosstrakh for 201 million rubles on September 7, 2001⁹. After the September auction, the privatization process stalled. However, on October 25, 2001, the Russian Deputy Minister for Property Affairs of Russia Mr. Braverman announced that the Government will sell 39% of Rosgosstrakh in a single lot. Thus, the government will retain 52% of Rosgosstrakh.¹⁰ The company is one of the leading insurers on the Russian market and it engages in the widest specter of insurance services, some of which are prohibited for distribution by majority foreign-owned insurers. The privatization scheme proposed in October of 2001 allows Rosgosstrakh to observe the

⁴ Pavel Miledin, Ingosstrakh is up for sale again, Vedomosti #202 11-01-2001

⁵ Interfax, October 24, 2001

⁶ Sergei Ul’yanov, International prize for Russian insurers, Rossikaya Gazeta #218 11-06-2001

⁷ Pavel Miledin, Ingosstrakh is up for sale again, Vedomosti #202 11-01-2001

⁸ Dmitri Sivakov Ingosstrakh’s fate, Expert #39 10-22-2001

⁹ Pavel Miledin, Rosgosstrakh’s version, Vedomosti #197 10-25-2001

¹⁰ Interfax, October 25, 2001

prohibition stipulated in the Law on Insurance. Rosgosstrakh possesses a huge countrywide infrastructure – almost 100 branches and 40,000 agents. However, these assets have not been properly accounted for; therefore the company is valued only at \$78 million.¹¹

Analysts conclude that Troika Dialog is working on behalf of a foreign player¹², in this particular case - AIG. In early 2002, Troika purchased a second lot in Rosgosstrakh during the privatization auction. Troika's management introduced new members to the Rosgosstrakh's board of directors. Troika's president also admitted that AIG was among the investors who formed the coalition to purchase the Rosgosstrakh.

¹¹ Dmitri Sivakov, Intervention is continuing Expert #34 09-17-2001

¹² Dmitri Sivakov, Intervention is continuing Expert #34 09-17-2001

Stakeholders

Russian Federation:

Ministry of Economic Development and Trade, Minister Gherman Gref.

The Ministry of Economic Development and Trade is responsible for the development of federal socio-economic policy of the Russian Federation. The Ministry also supervises, coordinates, and executes the process of Russia's accession negotiations in the World Trade Organization.

The Ministry drafts laws and comments on the proposed legislation that affects socio-economic development of the country.

The Minister officially chairs the new independent think-tank Center for Strategic Research (CSR). CSR produces first-rate economic research on issues related to the ongoing modernization of the economy.

Ministry of Finance, Insurance supervision department ISD

Ministry of Finance through its executive by-laws develops the legal framework for the insurance sector. The Insurance Supervision Department is the main regulatory/supervisory body for the insurance sector.

ISD openly denounces its role in formulating insurance policies – it performs only the supervisory function. However, the Insurance Supervision Department is known for its opposition to foreign companies access to the Russian insurance market.

Currently, the ISD is staffed with almost 200 employees but is unable to successfully perform all its supervisory functions. For example, licensing a company for operations in a certain sector takes more than two months, certification of insurance companies' managers also takes a long time. ISD used to generate insurance market statistics. All companies are required to submit information, financial statements, and to fill out special supervisory forms. ISD is the organization that possesses the most accurate and updated information about the conditions of the insurance market. Nevertheless, since 2001, ISD stopped providing statistical information about the insurance markets. ISD now only makes available the total numbers of premiums collected, and payments made in five insurance market sectors, as well as a breakdown of these numbers by the seven federal districts.

Prime Minister

Mikhail Kasyanov, the Prime Minister, and the former Minister of Finance, exercises strong influence over all divisions of the government. At the economic forum in New York, in February 2002, Kasyanov did not exclude possibility of amending legislation prohibiting majority-foreign owned insurance companies from operating in certain sectors of the Russian insurance market¹³.

¹³ Alexander Bekker Citibank and AIG want to expand business in Russia, Vedomosti #016 02-04-2002

If ISD cannot provide enough arguments for further protection of the insurance market, the Prime Minister will issue an order to reformulate Russia's position in the WTO negotiations.

The President

The Russian Head of State has enormous power and political clout in formulating the policies towards specific sectors in Russian economy. Vladimir Putin is the President who set the Russia's accession to the WTO as one of his highest priorities. Liberalization of Russian insurance market is likely to take place within the context of the WTO accession process. President Putin believes that accession to the WTO will positively affect the Russian economy.¹⁴

Earlier in the 2001, President supported the new tax legislation that exempts insurance expenses from income taxes. This was the beginning of a new policy toward insurance. "The Kremlin started to adopt industry policies founded on a reasonable consensus of domestic interest, instead of the favoritism and privateering of the recent past... when a single American insurance tycoon could purchase letters of demand from the U.S. Congress and State Department, hand-carry them to the Kremlin and the State Duma, and cash them at Boris Yeltsin's door into special favors for his Russian interest."¹⁵

The President not only exerts political pressure in resolving policy issues, but his Administration possesses \$600 billion in assets, some of that property requires insurance. The President's administration is also a big buyer in the insurance market. However, the insurance expenses are to be paid by the enterprises servicing the administration, rather than from the state budget.¹⁶

Federal Assembly

Federation Council

The Federation Council (the upper house of the Parliament) after 2001 reformed its procedures for electing its members, which consists of representatives from legislative and executive branches of power of the regions – subjects of the Russian federation. The executive branch appoints one senate member from each region, and the representative legislative body of every region selects another.

The Federation Council structures its work by committees, similarly to the work of the State Duma. The committee important to solving the problem at hand is the Committee of the Federation Council on Financial Markets and Money Circulation. Its chair, Serguei Vasilyev, was appointed by the government of the Leningrad Oblast' in 2001.

The State Duma

According to the Russian Constitution, the Duma is vested with the power to adopt and change federal laws. In the present political situation in Russia, the

¹⁴ Interfax, Russian president about WTO, 10-16-2001

¹⁵ John Helmer, "Putin bets on new policies for insurance", The Russia Journal June 29-July 05, 2001

¹⁶ Pavel Miledin Presidents administration is choosing insurers, Vedomosti #169 09-17-2001

Duma has been cooperating much more willingly with Putin's government on the issues of economic reform.

The Duma structures its work, as any other parliament, by respective committees. The Committee on Credit Organizations and Financial Markets (CCOFM) deserves special consideration. Its chair, Alexander Shokhin, is a member of the Duma faction "Peoples Deputy". The faction supports modernization of the Russian economy.

The Committee on Credit Organizations and Financial Markets contains the Insurance Subcommittee. The Insurance Subcommittee is led by Alexander Koval', a member of the Unity faction. Mr. Koval' is also the president of the All-Russian Insurance Association.

With the exception to mandatory insurance, the issue of liberalization of the insurance sector is not subject to party politics. Party politics become important only to overcome the Communists' resistance to the expansion of number of risks to be covered by mandatory insurance.

Table 1. State Duma factions:

Faction	Number of deputies	Faction's orientation
Unity	80	Pro-Kremlin, Supporting Government's policies, organized and led by President Putin's close ally S. Shoigu – Emergencies Minister of the Russian Federation
Fatherland-All Russia	44	Pro-Kremlin, organized by prominent governors, including Moscow Mayor Luzhkov and St. Petersburg's Mayor V. Yakovlev
Union of Right Wing Forces	37	Center-right, Supports the liberal economic reforms. Formed by the former Prime-Minister of Russia S. Kiriyenko, Former Deputy Prime-minister B. Nemtsov, and former Head of the Yeltsin Presidential Administration A. Chubais, current chair of the Russian energy monopoly Unified Energy Systems.
Liberal Democratic Party Faction	12	Organized by the scandalous right-wing politician V. Zhirinovskiy. Supports centralization, supremacy of the Russian ethnos.
Yabloko	19	Organized by the renown economist G. Yavlinskii who supports liberal economic reforms.
Communist Party Faction	85	Supports strong government regulation in all sectors of the economy. Opposes adoption of law on mandatory automobile owners insurance.
Agro-industrial group	42	Representative of the farming community of Russia. Opposes liberal reforms.
Peoples	60	Unites independent Duma members. Supports

Deputy		modernization of the national economy
Russian Regions	45	Assembled of the deputies elected from the Russian regions. Interested in establishing effective federation.
Non-affiliated deputies	19	

Russian Union of Insurers - All-Russian Insurance Association (ARIA)

Russian Union of Insurers unites the best specialist in the insurance field. Many top managers of Russian insurance companies lead working groups within the Union. In July 2001 ARIA’s president Igor Yurgens was nominated as vice president of the Russian Union of Industrialists and Entrepreneurs (RUIE)¹⁷.

In early 2002, ARIA decided to fight for status of independent federal regulatory body. ARIA proposes its own view of the appropriate policy toward the insurance sector. ARIA’s proposal does not contradict the policy proclaimed by the Government; however, it does not cover the introduction of free competition with foreign companies, or granting national treatment to foreign companies.

In February 2002, ARIA members elected a new president of the association – Alexander Koval’ – a current member of the State Duma. He belongs to the pro-president Unity party and does not plan to relinquish his Duma seat. In Duma he is an active member of the Committee on COFM, and a chair of the Insurance Subcommittee. Such a disposition provides ARIA with greater political leverage in the State Duma.

Russian Union of Industrialists and Entrepreneurs (RUIE)

RUIE was created to represent interests of the largest industrial enterprises and financial groups. Two other industrial associations were formed: OPORA (Union of Entrepreneurial Organizations of Russia) to represent the small enterprises and “Delovaya Rossiya” (Business Russia) to represent the interests of the medium-size enterprises. However, both these organization continue to lack political clout with the executive branch.¹⁸

The strength of RUIE lies within its board members who are regularly invited to update the President on the current state of the Russian economy as well as the current policy needs of the business community.

RUIE vocally supports Russia’s accession to the WTO. However, this support is not consensual; in RUIE there is a number of opponents to the WTO accession. The most vocal opposition comes from representatives of epy automotive industry, aerospace, financial services, telecommunications and agriculture.

Governors

Past development of the Russian insurance sector allowed for creation of small regional insurance companies that serve a certain region or a group of regions. Some of those companies are likely to face tough competition from foreign

¹⁷ Pavel Miledin “Yurgens decided to leave”, “Vedomosti” #160 09-04-2001

¹⁸ Alexei Germanovich “medium business behaves like big business” Vedomosti #191 10-17-2001

insurers. Governors of Russian regions could be interested in protecting those companies.

Federal legislation assumes universality of federal regulation of insurance throughout the entire territory of Russia. Governors cannot adopt regional insurance policies. Now, after the reform of the Federation Council, Governors will have even less clout with formulating the federal legislation.

Regulators of different mandatory insurance: firefighters, aviation safety etc. They are likely to be willing to retain control over the mandatory insurance flows associated with their agencies or the supervised economy sectors.

Foreign stakeholders:

American International Group

AIG is one of the leaders of the global insurance market, which operates in 130 countries. In most of the foreign markets AIG is involved in the life-insurance sector. AIG-Russia was created in 1991 and enjoys full, unconditional and irrevocable guarantees of the parent company¹⁹. Amendments to the law in 1999 did not affect either AIG or subsidiaries of Allianz AG. Both of these companies were able to grandfather their rights of working in both mandatory and life insurance sectors.

However, AIG-Russia was only able to become a leader in the Moscow regional market for long-term life insurance in 2001. Even though the company has the guarantees of its parent it is only an average Russian insurance company (#56, total premium collected in 2000). It appears that AIG has not been able to become a leader in the Russian insurance market even with the grandfathered rights to work in protected sectors.

Furthermore, these grand-fathered rights do not apply to new investments that AIG has made, namely Ingosstrakh and Rosgosstrakh.

The Government does not plan to fully privatize Rosgosstrakh. Therefore, it is unlikely that AIG's further investments will limit Rosgosstrakh's ability to work in all licensed sectors of the market.

Ingosstrakh's situation is different. Should AIG or other foreign investor acquire more than 49% of the company, Ingosstrakh will find itself excluded from both markets of life and mandatory insurance.

Allianz AG

Allianz AG is Germany's largest and the world's number three insurer. It has established a Russian subsidiary "Ost-West Allianz". "Ost-West Allianz" ranks 93 (in total premiums collected, sales) among all Russian Insurers.

In late June 2001 Allianz AG purchased 45% of ROSNO (Russian insurer #3, total premium collected 2000)²⁰. Allianz AG finds itself in a situation similar with the one AIG and Ingosstrakh have to face. According to the law, should the foreign-owned company acquire more than 49% in the insurance company, that

¹⁹ Pavel Miledin, Sistema has given up ROSNO, Vedomosti #176 09-26-2001

²⁰ Western Insurance companies Start entering Russian market
<http://lenta.ru/english/2001/06/28/insurance>

company automatically is excluded from a number of lucrative sectors of the market.

Besides from purchasing 45% stock in ROSNO, Allianz purchased an option to acquire more shares²¹. Allianz would be willing to execute the option in case the limitation on foreign participation is lifted.

ROSNO represents not only wide client base but it also has quite elaborate regional network of branches.

Igor Yurgens, in November 2001, quit his position as the president of ARIA and assumed a post on the board of directors at ROSNO²². Igor Yurgens is considered the strongest lobbyist for the insurance sector. Such a move can be interpreted that foreign capital (Allianz AG – owner of 45% of ROSNO) is hiring the best Russian talent to lobby the Russian Government and the State Duma for liberalization of the insurance market.

Acquisition of ROSNO by Allianz brings qualitatively new client base for ROSNO: foreign companies and their Russian branches. However, it is possible that ROSNO might lose its stronghold in mandatory insurance for federal agencies like Ministry for Taxes and Collections. It is unclear whether the Ministry will favor the fact the foreigners will have access to the data about its employees.²³

Foreign governments – members of the working party on Russia's accession to the WTO. The most interested WTO members are the United States, Germany, and the United Kingdom, Japan and Switzerland have also voiced concerns about foreign company access to the Russian insurance market.

²¹ Evgeni Reshetin, Intervention, Expert #25 07-02-2001 p 18-21

²² Pavel Miledin, Yurgens is leaving, Vedomosti #212 11-19-2001

²³ Evgeni Reshetin, Intervention, Expert #25 07-02-2001 p 18-21

WTO accession process

Russia submitted its services offer to the WTO negotiating group in early 2001 but received a “cool reception from key WTO members”²⁴.

With regards to the Insurance sector, Russian chief negotiator M. Medvedkov while commenting this submission at a press conference said, “Foreign insurers will also be prohibited from providing services linked with compulsory insurance and insurance connected with state procurement.”²⁵

On September 25, 2001, the Minister of Economic Development and Trade of Russia announced that informational stage of Russia’s accession to the WTO has been completed.²⁶ He stated that most trade in goods negotiations have been completed and one of the main contentious issues remains: services trade.

One of the services negotiation rounds took place in Geneva in early October 2001.²⁷ Later that month, a member of the Russian negotiating team announced that the financial services sector of Russia is the most prepared for WTO accession. Yet, the insurance sector’s limitations provoke the most protests from foreign counterparts.²⁸

Foreign counterparts actively support Russia’s accession process. WTO Director General Mike Moore expressed his support through promising his personal supervision of the accession process.²⁹

On September 24, 2001, Prime Ministers of Finland, Denmark and Estonia, who were participating in the Third Annual Baltic Forum expressed their support for Russia’s speedy accession to the WTO.³⁰

Chris Patten, EU’s Foreign Affairs Commissioner, and Pascal Lamy, EU’s Trade Commissioner, visited Russia in early December of 2001. The EU leaders are eager to engage in further economic dialogue. They support the idea of gradual engagement of Russia, according to which the WTO accession is an urgent and short-term task³¹. However, beyond the WTO accession, the EU is ready to consider widening economic ties into various fields of cooperation, including energy production (not currently on the WTO agenda.) The EU considers Russia’s

²⁴ Russian Official Defends WTO Market Access Offer, International Trade Reporter Vol.18, #10 p. 377

²⁵ Russian Official Defends WTO Market Access Offer, International Trade Reporter Vol.18, #10 p. 377

²⁶ Interfax, Informational phase for Russia’s joining WTO completed, 09-25-2001

²⁷ Kirill Palshin, Service for service, another WTO round, Izvestiya #185 10-06-2001 p.5

²⁸ Interfax, Financial sector is the most ready for WTO accession, 10-25-2001

²⁹ Interfax, Director General will personally supervise Russia’s accession, 12-10-2001

³⁰ Interfax, PM’s of Finland, Denmark, Estonia support Russia’s accession, 09-24-2001

³¹ Andrew Jack, Michael Mann, EU looks for sense in Russia trade dialogue, Financial Times 12-10-2001 p.10

WTO accession as a stepping-stone for achieving greater economic integration with its eastern neighbor.

The new American Presidential Administration is prepared to help Russia become a member of the WTO and stresses economic cooperation with Russia as a key to improving relations with the U.S.³² The United States has progressed more in the negotiations with Russia than any other member of the WTO. It is ready to consider Russia to be a country with market economy³³ and to is ready to support a consideration of a working party report as early as December of 2001.³⁴

Although US trade representative Robert Zoellick stated that it was erroneous to seek a geopolitical reason for speeding up Russia WTO accession³⁵, some political observers see the linkage between Russia's support of anti-terrorist operations in Afghanistan and consideration of its WTO application³⁶ by the western counterparts.

WTO popularization conferences experience

Throughout 2001, the government of Russia conducted a series of informational WTO accession business conferences in different regions of Russia. The intent of these conferences was to familiarize the business community with what the WTO accession will mean to Russian business as well as to generate new input from the regional business community as to what should be the priorities for Russian WTO accession negotiations. The general outcome of these conferences was that the business community supports the WTO accession. The business community's support is reflected in the statements by the RUIE and other business lobbying entities.

³² Washington Trade Daily, August 1, 2001, p.5

³³ Georgii Osipov, Come in to trade, we have a chance of becoming WTO member. Izvestiya, #181, 10-02-2001 p.6

³⁴ Interfax, USA is ready to discuss working party report in December, 09-28-2001

³⁵ Interfax, USTR refutes political reason for speeding up Russia's WTO accession, 09-28-2001

³⁶ Guy de Joquieres, Rafael Behr, Anti-terrorism group gets behind Russia's plan to join WTO, Financial Times, 10-24-2001, p.12

Current Insurance Policies

The official government position on insurance is recorded in the laws about insurance and related legislative acts. However, analysis of these obsolete acts is more relevant for the legal analysis section rather than for the current section. This section will focus on the recent developments, which have not yet been enacted into legislation.

The Government of the Russian Federation proposes the following as the major economic policy in the insurance sector³⁷:

- Creation of national insurance system that would be able to perform the following socio-economic functions: protection from potential risks necessary for effective functioning of market economy and for stimulating entrepreneurial activities;
- Accumulation of long-term investment resources within Russia.

Among the main objectives for the insurance sector the government names the following:

- Creation of the adequate legal framework for the insurance sector;
- Creation of the effective mechanism of state regulation and supervision, what is very important during the period of formation of national insurance system;
- Development of mechanisms for transforming consumer savings into long-term investments by utilizing mechanisms of life insurance;
- Step by step integration of the national system into an international insurance system.

The Government program proposes a number of practical steps for achieving these goals: establishing systems of mandatory insurance (like automobile owners liability; a law that will expand the insurance market by \$1 billion, is under consideration by the State Duma³⁸) and mandatory state insurance, which amends tax laws to exempt insurance payments from immediate taxation etc. These policies deal mostly with the domestic aspect of the Russian insurance sector.

The Russian government is developing new legislation to eliminate the use of life insurance for schemes to avoid payroll taxes.³⁹ Currently budgets at all levels suffer from shortage in collection of taxes due to the fact that enterprises abuse life insurance schemes to avoid taxation. Experts estimate that only 25% of life-insurance premiums collected actually represent true life insurance business, while the rest is used to reduce the tax burden. The tax “savings” amount to 25-35% of the life insurance premiums paid.

³⁷ Main objectives of socio-economic policy of the Russian Federation, Center for Strategic Research, 1999-2000, www.csr.ru

³⁸ Pavel Miledin “\$1 billion is on the bid” *Vedomosti* #195 10-23-2001

³⁹ Intrefax, December 7, 2001, the government will fight the tax evasion life insurance schemes

Exclusion of health insurance

The Ministry of Finance in its effort to streamline the regulation of insurance has ceased regulation of 300 health insurance companies that did not insure any other types of risks by mandatory health insurance. The Ministry believes that the health insurance business is not strictly insurance business and therefore does not require direct licensing and regulation by the Ministry⁴⁰. The official policy on medico-social insurance is to be stipulated in the new law on medico-social insurance. The Ministry of Economic Development and Trade is drafting that law.

The last two domestic policy issues related to the development of the insurance sector are:

- Taxation policy in terms of the ability for enterprises to write off insurance expenses as tax deductible; and
 - Policy towards mandatory insurance.
- These topics will be more fully considered in the Legal section.

⁴⁰ Pavel Miledin, Why does ministry of finance need the insurers? Vedomosti #214 11-21-2001

Legal Framework

Russia is a federal state; therefore, it delegates authorities and competence between federal government and regional governments. Unlike in the U.S. insurance sector in Russia like other financial services sectors is regulated only by the federal legislation and controlled by the federal supervisory bodies. Federal laws and presidential decrees are binding throughout the territory of Russia. The federal government has exclusive competence over specific areas, such as foreign investment in the financial, monetary and credit sectors. The Ministry of Finance through its Department of Insurance Supervision regulates the activities of all insurance companies.

Russian domestic legislation with regard to insurance consist of the following:

- a. The Law “On Organization of Insurance”;
- b. Civil Code (selected articles) The Civil Code of Russian Federation regulates several important aspects relevant to the insurance sector.
- c. Tax Code (selected articles); and,
- d. Finance Ministry by-laws.

In 1992, the State Duma adopted the original Law of the Russian Federation on Insurance. It was amended in 1999 to include the aforementioned prohibition on the sale of mandatory insurance by majority foreign owned companies.

Legislative history shows that due to enormous lobbying pressure that Russian companies were able to exert on the State Duma, the Duma was forced to pass the discriminatory law. Yeltsin’s government either considered preservation of competition rules in the sector as unimportant or was unable or unwilling to overcome the lobbying pressure.

Main protectionist norms of the law, as outlined in the Issue section, are stipulated in the 1992 (as amended in 1997 and 1999) Federal Law “On the Organization of Insurance”. Stipulations of the regulations issued by the Ministry of Finance are just fulfilling the meaning of the Federal Law.

Article 6 (Insurers) of the Law “On the Organization of Insurance” stipulates that foreign owned insurers cannot sell life and mandatory insurance, as well as insurance for governmental needs.

It is important to understand the political layout that existed on the moment of adopting the last version of the Law. In 1999, President Yeltsin’s Administration submitted a draft text on insurance law to the State Duma. The original text was heavily influenced by the ongoing Russia’s negotiations for the WTO accession. It was a rather liberal text allowing for greater foreign participation in the insurance sector.

However, lobbying pressures from domestic insurance companies were sufficient to overcome the President's veto and institute a protectionist regime on trade in insurance.

The new law did not affect rights of existing foreign insurance companies. Their life insurance and other licenses were grandfathered. Such grandfathering took place only after numerous American lobbying groups for financial services undertook an effort to lobby the executive and legislative branches of the Russian government.

Consequences of possible Russia's WTO accession and its possible obligations under GATS

In compliance with GATS requirements, Article 15 of the Russian constitution stipulates that all legislation, regulations and administrative practices must be published; and can only enter into force when published. The fact that applicable legal texts co-exist with its frequent amendments often leads to ambiguity and make interpretation difficult, especially for foreign businesses.

The Russian political culture has historically lacked effective lobbying mechanisms. Only recently have large, medium and small enterprises, as well as industrial groups, started to form legislative consulting bodies to more fully participate in the legislative process.⁴¹

To comply with provisions of Article VI of the GATS, Russia will have to reconsider the economic rationale underlying the current regulation in the insurance sector and define more clearly the functions of its regulating agencies. The new legislation should limit the bureaucratic discretion. Russian authorities admit that the implementation of GATS commitments offers a good opportunity to implement a solid legal structure, which is compatible with international practices. Nevertheless, Russian authorities would like to preserve a certain degree of flexibility to be able to adapt legal structures necessary for rapid development of the services sector.

With regard to Article V (Economic Integration) of the GATS, Russia and its negotiation partners must examine the following. Russia will have to clarify status of agreements concluded with the partners of the Commonwealth of Independent States (CIS) and assess their consequences for the application of MFN treatment. The Treaty on the Creation of the Economic Union concluded in September 1993 by CIS countries covers trade in goods and services and also concerns commercial presence. Furthermore, Russia has concluded more than 700 agreements with individual members of the CIS. Some of these agreements may be relevant to trade in services and imply preferential treatment in terms of one or more modes of supply. Due to the large number of agreements it is difficult to compile an

⁴¹ Formation of Russian Union of manufacturers and Industrialists or medium size business' "Delovaya Rossiya" along with ARIA are good examples of such new lobbying institutions.

exhaustive list of preferences granted by Russia. Due to the economic weakness of the CIS members it is unlikely that Russia will have to negotiate the degree of flexibility to grant them preferential treatment in the insurance sector.

New tax regulations

As of January 1, 2002 property insurance expenses are fully tax deductible. From the standpoint of insurance the sector it is the main accomplishment of the drafters of the new Chapter 25, Part II, of the Russian Tax Code. New legislation allows writing off mandatory and voluntary insurance payments as tax-deductible expenses. Almost all insurance expenses are excluded from income taxation.

Personal insurance payments have been excluded from taxation but with a few exceptions. These limitations were introduced to counter the misuse of personal insurance as a scheme for tax evasion. According to the new law, long-term life insurance premiums paid by the employers cannot exceed 12% of total payroll.

However progressive this new regulation might be, domestic insurers still criticize it. The main reason for criticism is the inconsistency of dates in tax accrual for different types of insurance contracts.⁴² Resolution of this problem is possible in conjunction with a comprehensive accounting reform, which is another hot topic of political debate in Russia.

Currently, there is no single unified mandatory insurance law that would set the guidelines for provision of mandatory insurance.

Auditors liability insurance

In September of 2001, the new federal Law on Audit entered into force.⁴³ The Law on Audit obliges auditors that conduct mandatory audits to insure their possible liability for breach of contract. However, the law does not stipulate the minimum limits or conditions of such insurance. As much as 60% of Russian auditors insure their liability to clients. Six companies have liability coverage exceeding \$1 million.⁴⁴ Experts estimate that total market for this sector will amount to \$1-1.5 million annually.⁴⁵

Automobile-owners liability insurance

The Specialized Committee of the State Duma has recommended that the Duma pass the law on mandatory car-owners liability insurance. The law was adopted in the first hearing in April of 2001.

Insurance companies will have to acquire a mandatory insurance license to operate in this new market, but the government will exclusively set the rates. The

⁴² Insurers are satisfied, Expert #34 09-17-2001

⁴³ You will have to pay for mistakes, Expert #34 09-17-2001

⁴⁴ You will have to pay for mistakes, Expert #34 09-17-2001

⁴⁵ Pavel Miledin, Auditors will be insured. Vedomosti #163 09-07-2001

rates set by the Government should not exceed \$10-20 for coverage of 400,000 rubles (\$13,000)⁴⁶.

The main issue of debate is the status of the Guarantee Fund. The Fund's purpose is to make payments when it is impossible to determine fault in the accident or in case of bankruptcy of the insurer. Insurance companies will be required to remit 5% of collected premiums to the Fund. Legislators are still discussing the principle scheme of the Fund and will not resolve the issue until mid 2002.⁴⁷

⁴⁶ Pavel Miledin "\$1 billion is on the bid" Vedomosti #195 10-23-2001

⁴⁷ Interfax, State Duma will postpone consideration of Insurance law, 12-10-2001

Economic Analysis

What economic rationale is to be overcome in the coming discussion?

Opponents of the opening of insurance markets to foreign participation state the following as the major reason for supporting their cause:

Foreign insurers collecting huge premiums (in the developed countries up to 10% of GDP), will transfer the collected premiums, that otherwise would be invested in the domestic economy, abroad. Insurers do it through a number of channels: reinsurance, investments of premiums in foreign capital markets, and repatriation of profits.

This argument is unviable since Russian companies contribute to the outflow of capital in through exactly same mechanisms, except maybe for the repatriation of profits, which domestic companies retain in Russia or distribute to domestic shareholders.

Currently, the Russian economy is grossly underinsured. The proportion of insurance in the overall economy is very small. There are three measures of insurance penetration:

- *Percentage of premiums collected in the GDP.* In 2000, Russia collected insurance premiums that equaled 171 billion rubles⁴⁸. Russian GDP in 2000 amounted almost to 7 trillion rubles. According to these figures insurance penetration of Russian economy is 2.44%.
- *Ratio of Insurance companies capital to the overall capital in the country.* Since insurance companies face limitations on the minimum size of capital and face strict licensing and reporting requirements, total capital of insurance companies is easily determinable and amounts to \$1 billion. Overall capital invested in Russia is not easily determinable. Conservative estimates suggest \$50 billion figure.⁴⁹ These figures still produce the same level of insurance penetration of the Russian economy – 2%.
- *Consumer insurance spending* in Russia is very low: “in 1997 Russian citizens paid \$43 per capita in insurance premiums. The 1998 crisis reduced premiums to \$29. In comparison, in Estonia, the current estimated insurance per capita spent is \$60; Turkey \$200; Slovenia \$350. In Western Europe, the range is between \$1,000 and \$2,500; in the United States, \$3,000; and in Japan, more than \$4,000.”⁵⁰

Insurance penetration ratios are very small for Russia when compared to the transition economies of Eastern Europe. Eastern European countries commit an average of 5% of their GDP's toward insurance premiums. When compared to OECD countries the difference in insurance penetration ratio is even greater. On average that ratio is between 8 and 10%.

⁴⁸ Ministry of Finance of Russian Federation website : <http://www.minfin.ru> visited on 11/25/2001

⁴⁹ John Helmer, “Boom for Industry as Russia gets insured” the Russia Journal May 25-31, 2001

⁵⁰ John Helmer, “Boom for Industry as Russia gets insured” the Russia Journal May 25-31, 2001

The main reasons why the insurance penetration ratio for Russia remains small is the overall poverty of the population, weak financial health of domestic enterprises and no traditions of using insurance services.⁵¹

Apart from direct investment, foreign insurance companies are present in the Russian market through the reinsurance. Reinsurance payments made to foreign companies withdraw capital from the country. Reinsurance capital outflows contribute to the decrease in the total capital available for investment in Russia. Total outflow of capital in the first half of 2001 exceeded \$10 billion.⁵² In 1999, the Russian reinsurance balance of payments had a deficit of \$283 million, in 2000 it totaled \$450 million.⁵³

After the September 11, 2001 terrorist attacks on the U.S. and the enormous losses acquired by the global leaders in the insurance sector, reinsurance for Russian companies will become even more expensive. Some Russian insurers estimate 10-20% increase in reinsurance rates for property insurance and cannot make estimates for reinsurance rates for air travel and other risks.⁵⁴

Another reason for increase in the reinsurance premiums is the new tax legislation described in the legal framework section.

Despite inadequacies in the development of the Russian insurance market, the market itself is growing rapidly:

Table 2. Premiums Collected

	1998	1999	2000	2001
Number of companies	1408	1294	1167	1064
Total premiums collected, Rubles, billion	42.7	96.6	171.0	276.6
Life insurance, Rubles, billion	12.4	35.5	79.8	139.7
% of total	29.1	36.8	46.7	50.5
Liability insurance, Rubles, billion	1.5	4.5	6.6	9.2
% of total	3.4	4.6	3.9	3.3
Mandatory insurance, Rubles, billion	14.5	21.5	30.4	40.3
% of total	34.0	22.3	17.8	14.6

⁵¹ All-Russian Union of Insurers, Bulletin of the Committee for Foreign Affairs #3 2001, p.14

⁵² Interfax, Russia's capital flight, 10-25-2001

⁵³ All-Russian Union of Insurers, Bulletin of the Committee for Foreign Affairs #3 2001, p.10

⁵⁴ Pavel Miledin "Without insurance", Vedomosti #174 09-24-2001

The number of companies in the market decreases over the years. This fact reflects continuous market concentration. Over the past three years concentration of capital in the insurance market has become increasingly larger. The total number of insurance companies declined from 1408 in 1998 to 1140 in September of 2001.⁵⁵

If in 1999 264 companies collected 90% of total premiums, in 2000 the same proportion was collected by 233 companies (21% of total number of the insurance companies).⁵⁶

Life insurance

Steady increase in the share of the life insurance premiums collected represents merely the increasing use of tax avoidance schemes. Use of life insurance for avoiding payroll taxes is described in the policy section. Currently, some leaders of the insurance market, for example Rosgosstrakh, are limiting their participation in such schemes.

It is the official policy of the ARIA to reduce the use of tax avoidance schemes. Otherwise, the regulators and the government as a whole perceive insurance companies to be sheltering a large share of clients' payroll spending from payroll taxes.

Liability insurance

A decreasing share of liability insurance while the total amount of liability insurance premiums is growing reflects the same disproportionate growth of the life insurance sector. Experience gained in the liability sector is vitally important to the development of the mandatory insurance sector, since most of the mandatory insurance stipulations cover third party liability risks.

The statistical numbers provided by the Ministry of Finance combine health insurance, mandatory state insurance and mandatory insurance under one category: mandatory insurance. A large share of that is health insurance. In 2001 mandatory health insurance premiums amounted to 37.8 billion rubles⁵⁷. Mandatory state insurance and mandatory insurance amount to 2.5 billion rubles, or .9% of the total market. Mandatory state insurance is paid by the federal or local budgets and is accounted for in the 2.5 billion rubles of premiums collected in 2001.

Non – state mandatory insurance is a still very small sector of the insurance market. However, it is poised to multifold, after the adoption of automobile owners liability law (~1billion dollars).

⁵⁵ Ministry of Finance of Russian Federation website : <http://www.minfin.ru> visited on 11/25/2001

⁵⁶ All-Russian Union of Insurers, Bulletin of the Committee for Foreign Affairs #3 2001, p.7

⁵⁷ Ministry giving up regulation of health insurance



Figure 1. Proportion of non-health mandatory insurance



Figure 2. Proportion of non-health mandatory insurance including automobile owners liability insurance

Gains from foreign participation can be achieved in several ways:

- Inflow of additional capital to the insurance sector
- Transfer of technology, experience, and education
- Introduction of price competition

Technological gains

Transfer of extensive foreign experience is possible in two ways:

Implementing new technologies and training local staff: Some foreign insurance companies have been in the market for ten years now. However, their combined share in the total insurance market is only between 5 and 7%. AIG is the leader among foreign insurers in the Russian market. It employs approximately 200 people in Moscow headquarters and has a small network of agents. Such small numbers of personnel, even trained to the high standards of providing insurance services, are not sufficient for generating enough expertise among the entire insurance community to effectively upgrade the knowledge to the new standards.

Another way in which technological gains from foreign competition could be advantageous for the Russian market is through participation of foreign experts in developing regulatory agencies (either state or independent) and procedures. Experience shows that foreigners have been shut out or have not participated in the functions of the ARIA. Statistical surveys in some instances exclude AIG and some others from the list of market participants.

In order for the technological transfers from the foreign insurers to become effective there is a need for foreigner participation in managing the large insurers (top ten) with extensive branch and agent networks. Such participation will facilitate the transfer of new technologies and standards to a much larger number of specialists, which in its turn will cause a spill over effect to the rest of the market. Larger insurance companies have a bigger stake in efficient regulation, as well as they have greater political clout in developing the regulations with either state or self-regulating regulatory body.

Price competition.

Another advantage of the foreign competition in the insurance market is in price competition. Foreign companies have larger reserves. This enables them to set insurance rates lower than domestic companies. There are possible negative consequences for such price competition, as foreigners might have tendency to abuse financial leverage of their huge parent companies to pressure locals out of the market.

However, price competition in the mandatory insurance sector is not as likely as in the rest of the market. The payout ratio for mandatory insurance, excluding mandatory health, is 68%. This is higher than the total payout ratio for the entire market at 62%, or the payout ratio for voluntary liability insurance at 9% and voluntary property at 15%. Mandatory insurance is not a likely sector for intense price competition.

**Foreign experience in insurance liberalization:
Hungarian insurance market experience**

The Hungarian insurance market was completely monopolized until 1952. After the prohibition of private property and entrepreneurship was lifted in 1956 voluntary insurance grew significantly and a wide range of property risks were covered: houses, small farms, and later automobile. The Hungarians developed a combination of personal insurance plans, including life, medical, casualty, for groups or families for relatively small premiums.

Although a new economic regime was introduced, the state monopoly in insurance existed throughout 1986. From the time between 1950-s till the middle of 80-s the state insurer was able to develop excellent network of agents (7000) and has developed some insurance expertise.

1986 became the year of demonopolization in the Hungarian insurance market. Former state insurance was divided into two companies: Hungarian Co. and State Insurance Co. In turn, these two companies created a larger number of specialized companies. At the same time, state insurance supervision was instituted and market was opened for participation of foreign insurers. Foreigners could now own 100% in an insurance company, however, until 1996 special permission of the Council of Minister was required.

Between 1986 and 1995, minimal requirement for capital was one billion forints (1986 - \$20mil; 1994 - \$9mil). High minimal capital requirement enabled companies to acquire licenses simultaneously in different sectors of the market. Between 1990 and 1991, eight new companies entered the market.

The next stage of the development of Hungarian market brought privatization of the two former monopolies. Allianz AG bought Hungarian Co. and Dutch AEGON Group purchased State Insurance. 1991 was the year of significant increase in competition. Over the years, the market share of the two largest companies has been waning and currently represents about 50%. Concentration of Hungarian market has been declining as well:

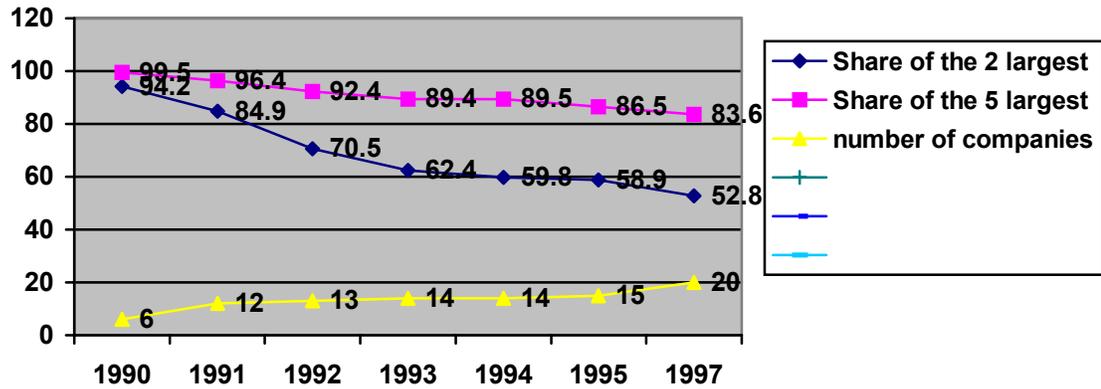


Figure 3. Insurance market concentration in Hungary
New insurance legislation in 1996 separated the companies into life and non-life separate insurance businesses. The legislation introduced different levels of minimal capital requirements for different market sectors.

Table 4. Premiums collected in Hungary, \$millions

Year	Total	Life	Non-life
1988	496	69	426
1992	744	97	647
1993	803	138	666
1995	944	278	666
1996	997	315	682
1997	1055	344	711

Positive results of attracting foreign capital to the insurance market in Hungary:

- Additional capital
- Technological transfers
- Increased quality of service lower costs
- Better insurance regulation
- Significant share of investments by the insurers remained in Hungary.

Possible problems of foreign company access to the Hungarian insurance market:

- Excessive repatriation of earnings or capital directly or through reinsurance
- Powerful foreign investor can outweigh the state regulator or supervisor
- Large companies might create new monopolies.

Commercial Analysis

As of the December 2000, forty companies with significant foreign participation were registered in the Russian insurance market. Their capital in the total capital of all Russian insurance companies did not exceed 5.3%. However, there is steady increase in the amount of premiums collected by foreigners in the Russian insurance market. Their share in the premium collected has grown from 6.0% in 1998 to 8.4% and 9.9% in 1999 and 2000, respectively.⁵⁸

Table 5. Major foreign insurance companies present on the Russian market:

Foreign Parent	Rank among world insurers, premiums collected	Russian Subsidiary	Rank in Assets (rank in premiums collected), 2000
Allianz AG – Germany	3	Ost-West Allianz,	- (93)
		ROSNO	6 (3)
AIG - USA	7	AIG Russia	- (56)
		Rosgosstrakh	5 (7)
		Ingosstrakh	1 (9)
Pohjola		Principal	
AXA – France	1	Renaissance-Insurance	17
Zurich financial services – Switzerland	8	Zurich –Rus’	75
ERGO insurance group (Munich Re) – Germany	9	Rus’	58 (88)
Swiss Re - Switzerland		Sun Life Rus’	

As described in the Background section, AIG and Allianz are actively acquiring large Russian insurers with well-developed branch and agent networks, and significant market knowledge, such as ROSNO, Rosgosstrakh, and Ingosstrakh.

Allianz AG is engaging in acquisitions all over Eastern and Central Europe. On October 23, 2001 Allianz and UniCredito (second largest Italian Bank) bid for the entire voting stock of Zagrebacka Banka, Croatia’s biggest bank.⁵⁹ Allianz partial overtake of ROSNO indicates that Allianz may attempt to establish control over significant share in the Russian insurance market, once the appropriate regulations are in place.

⁵⁸ All-Russian Union of Insurers, Bulletin of the Committee for Foreign Affairs #3 2001, p.9

⁵⁹ Tony Mayor, Fred Kapner Allianz, UniCredito in Croatia deal, Financial Times October 24, 2001, p.22

July 2003 is set as the starting date for Automobile mandatory insurance law. Automobile related risks usually are the first ones that a person has to insure independently. The practice shows that customers of insurance companies tend to return to the same insurer, with which they had positive experience in insuring automobile related risks. The company that provided satisfactory service in automobile insurance gains new clients for other lines of business. Foreign insurers are interested in gaining access to the mandatory insurance market some time before July 2003, in order to participate in training roughly 20 million automobile owners in using insurance services.

The introduction of the mandatory insurance law will not exclude major players such as AIG and Allianz, from the automobile insurance sector. Share of their subsidiaries in the total market is insignificant. AIG's and Allianz's current interest lies with expanding ownership in the Russian insurance giants – leaders of the market, specifically, ROSNO, Rosgosstrakh and Ingosstrakh. Acquisition of a share exceeding the 49% threshold will affect a number of current licenses issued to these firms.

Legal analysis

The 1992 Russian Insurance law, as amended in 1999, is this project's commercial issue.. Amendments to the provisions of this legislation will provide a solution for foreign access to the protected sectors. However, an amendment to that legislation does not guarantee a long-lasting solution, because of the new elaborate insurance legislation being developed.

The government is drafting several laws that will affect the mandatory insurance market and market access for foreigners. Included are:

Insurance Law, which will replace the existing discriminatory and outdated legislation;

Law on Mandatory Insurance, which will streamline the state regulation of mandatory insurance by setting overall principles of mandatory insurance, leaving detailed regulation to the state or independent regulator. This law will also remove the supervision and regulatory function from numerous governmental agencies supervising activities, which by nature and by law require mandatory insurance. Currently there are about 40 types of mandatory insurance that are supervised by various agencies.

Law on State Supervision and Regulation of Insurance – will determine the competencies of the state regulator. Participation in drafting this law provides a possibility to include the self-regulating body provision. The Ministry of Finance is likely to try to reduce the competences, if allow them at all, of any independent regulatory body.

Possible law on Self-regulating body in insurance

Due to large number of risks that are likely to be included in mandatory insurance legislation, it is logical to adopt a single federal law about the principles of insuring mandatory risks. Such a law will solely list the risks, allowing the regulator, either independent or state, to set the rules for the market.

The legal solution to the commercial issue at hand will be in influencing the development of the new Insurance legislation and a new law on mandatory insurance. Provided that appropriate stipulations are included, these legal instruments will help foreign companies secure access to the Russian mandatory insurance market.

Political analysis

Who are the likely allies and what interest should be addressed to mobilize their active support?

Stakeholders who gain from liberalization of the mandatory insurance market, coupled with the WTO accession, are:

The Russian industries that receive access to the foreign markets (RUIE).

Russian Union of Industrialists and Entrepreneurs openly supports a speedier Russia's accession to the WTO. Few business people have enough courage to openly criticize the President and his policies. However, there are factions within the RUIE that oppose WTO accession. Specifically, the aluminum group SibAl and Russian Aluminum group headed by Oleg Deripaska, who controls Russia's #2 car manufacturer GAZ and a number of bus production enterprises. He will try to protect his automobile manufacturing interest. Other industries with strong lobbies include aerospace, furniture-making, financial services, telecommunications and agriculture.

Gains from speedier WTO accession are apparent to the members of the RUIE; however, it is important to point out specifically the gains from more efficient operation of the insurance market. There are certain gains to be achieved through price competition, especially in the voluntary liability and property insurance sectors. Nobody else but the Russian business community will realize these efficiencies. Foreign competition also brings vast experience that translates into new insurance products available to the growing business community in Russia.

Some of the oligarchic structures represented in the RUIE possess their own captive insurance companies. WTO accession will make possible better operation of the Russian captive insurance companies abroad, where they would be able to follow operations of the industrial holding parent.

As stated earlier, ARIA plays a significant role in the work of RUIE. ARIA's support for the proposed opening of the mandatory insurance market will be magnified by the support from the RUIE.

The President: President Putin has set the accession of Russia to the WTO as one of his administration top priorities. Russia's accession will be perceived as a success to his foreign policy, and will help in his 2004 reelection. His Administration is also interested in a balanced economic development of the country; and thus in the development of insurance sector.

President Putin is able to exercise enormous pressure within any branch of the federal government. The Unity Party, with a strong faction in the Duma, will be instrumental in delivering the President's message to the legislators.

Should ARIA be greatly dissatisfied with the opening of the mandatory insurance market to foreign access, ARIA as a whole and a portion of RUIE will cease their

support for the president's policies. To avoid political liability for the president it is necessary to deliver ARIA's support to him.

If ARIA supports the opening of the insurance market as a part of WTO accession, Putin will be able to influence the Duma to accept WTO accession package. If the insurance market liberalization will be separated from the WTO accession and facilitated through a broader insurance development legislation, then his political power will still be vital to push through the necessary laws.

Foreign insurers

Foreign insurers currently operating in the Russian market among which are: AIG, Zurich Re, Munich Re, Allianz AG and others are interested in the speedier access to all sectors of the Russian insurance market. Although a number of their subsidiaries were granted licenses at the beginning of the 1990's and those licenses were grand-fathered in 1999, meaningful expansion is possible for them only through acquisition of established Russian insurance giants such as ROSNO, Ingosstrakh, Rosgosstrakh, and others. The political situation when foreign insurers were able by buying political pressure on the President's Administration and on the State Duma to extort market concessions has passed. Under the current regime, foreign companies as well as their subsidiaries must operate under the single set of rules. The best venue for addressing the problems they encounter with regulators is through participation in the domestic industry associations.

The greatest strength foreign companies have is their lobbying influence on their respective domestic governments. Foreign insurers can participate in the formulation of WTO members' negotiating positions, as well as negotiating instructions. Foreign insurers could become a channel to communicate with the WTO working group counterparts.

Aside from market access, foreign insurers could be interested in participating in the formulation of insurance policies and insurance regulation along with supervision. Independent self regulating body is established in compliance with WTO rules will be open to participation by foreign investors. Participation of foreign companies in such a body will become beneficial not only to them but to other participants of the market.

Foreign governments- members of the accession negotiations group

Who are the likely opponents? What are their strengths? Which of their interests need to be addressed to neutralize their opposition?

Ministry of Finance, ISD: ISD traditionally has been opposed to opening the insurance market. This opposition follows from the times when ISD used to be a close ally of the insurance community.

Among the strength of the ISD is the fact that they currently control the issuing of new licenses and have the power to withdraw existing licenses.

Within the inter-governmental discussion of the WTO accession process, the Prime Minister wants to see consensus being built among the different ministries on the negotiating position. As to allowing foreign access to the mandatory insurance market, the PM will exercise his power to relax this requirement in case major players exhibit a consensus to open up this particular sector. ISD cannot effectively function within the current budgetary and staff constraints. Reform of the state regulation of insurance is needed. ARIA is ready to take over a part of the regulation. Delimitation of regulatory functions will create mechanism for cheaper and more streamline regulation. This in turn will help the ISD to remain in the budgetary constraints while becoming effective regulator rather than a burden on the insurance community.

Another factor that has to be considered in approaching the issue of more effective regulation is the monetary compensation for the supervisory body that according to the proposed law is planned to be 0.1% of all insurance premiums collected. For 2001 alone, this figure would amount to \$9 million. Should ARIA become a SRB it will contest the allocation of these resources at least to some extent. However, even a portion of this sum will be a great benefit for ISD to improve their work.

All-Russian Insurers Association

Should ARIA become a self-regulating body, it could perform some of the functions of ISD, which it does not handle adequately. Among those: statistical information gathering and analysis, certification of the management of the insurance companies that seek government approval for licenses, product approval.

When committing our Ministry's support for ARIA's status as a self-regulating body, the Ministry representatives have to make sure that such SRB is WTO consistent. SRB cannot become protectionist body, it has to be open to all participants in the market, without prejudice to the size of capital, nationality, type of license, size or geographic sphere of operations.

As very few people in the State Duma really understand the WTO accession process, no serious party divisions could be expected on the issue at hand. It will be sufficient to gain influence from the specialized committee.

Legislative history⁶⁰ shows that there is little or no party division in the State Duma on the issue of insurance. As recent as 1999, when the insurance legislation was last heard in the State Duma, a vote occurred immediately after the

⁶⁰ Transcripts of plenary session of the state Duma.

presentation of the Financial Markets Committee chair without any deliberations. The legislative reconciling work is done in the Committee, and most of the deputies voted as the majority of the Duma membership.

The main opposition to the mandatory insurance legislation will come from the Communist Party faction, and their possible allies in the Agrarian party. The State Duma Subcommittee on Insurance is chaired by the Unity Faction member, Alexander Koval', and current president of ARIA. Among the members of the larger Committee on Credit Organizations and Financial Markets Vladimir Tarachev is another active proponent of the insurance business interests. Mr. Tarachev also belongs to the Unity Faction. Other members in this committee are not active in the politics of regulating the insurance sector.

Such disposition, even though not free of an internal conflict of interest, still represents dual possibility for advancing the cause of liberalization of mandatory insurance in the State Duma. Alexander Koval', as the president of ARIA, represents the interests of the insurance community. At the same time in order to observe his party loyalty he has to advance the policy of pro-President Unity faction. Should Koval' be engaged as the president of ARIA in reforming the rules for foreign access to the mandatory insurance market, he will become engaged as the chair of the insurance subcommittee in the State Duma.

Party loyalty of both Koval' and Tarachev will help advance the insurance policies supported by the President and the Government, assuming ARIA's approval on any such policies. Such an approval is required for the possible passage of any insurance law, because these two members, Koval' and Tarachev, will be able to stall the work on the subcommittee level.

Committee Chair Alexander Shokhin, an active member of the Peoples Deputy faction has accepted the position of vice president of Renaissance Capital investment bank. His resignation of the chairman seat will not result in major change in the outlay of political forces in the Committee. Committee chairs' seats are distributed according to the negotiated agreement among the different factions, so the chairman seat will be transferred to another Peoples Deputy faction member.

It is important to illustrate which Duma factions are likely to support the Unity Faction in adoption of the relevant legislation on insurance. If we analyze the votes on the economic package of laws, we will see that the Unity Faction position was supported by the following factions in these proportions.

Table 6. Support for Unity Faction position.

Faction	Number of laws on which position coincided with Unity Out of 28 laws	Percentage of coincidence, as measure of support

	support by Unity)	
Fatherland- All Russia	25	89.3%
Peoples Deputy	25	89.3%
Russian Regions	22	78.6%
Yabloko	20	71.4%
Union of Right Wing Forces	18	64.3%
Liberal Democratic Party Faction	14	50%
Communist Party Faction	13	46.4%
Agro-industrial Group	13	46.4%

Undecided / remotely related stakeholders:

Populace

Traditionally, the public views insurance as a form of tax. Examples include social security (pension insurance) and mandatory health insurance (tax to finance the state medical care system). Such perception leads to two outcomes: low insurance culture – many risks remain uninsured and to opposition by the majority of the public to expanding mandatory insurance. Specific to the issue at hand is the law on mandatory automobile owners third party liability. It envisions that universal base rate for automobile owners will be around \$50 annually. This law is likely to draw public discontent, as this base rate represents about 3% of average annual wage in Russia. Politically, the Communist Party and its faction in the State Duma oppose the adoption of such a law, claiming that this insurance will be ineffective and become another form of tax on automobile owners.

Other regulators:

Current regulators of the mandatory insurance including among others the following governmental agencies Defense Ministry, Fire Service of the Emergencies Ministry, agency supervising aviation mandatory insurance, Natural Resources Ministry supervising environmentally risky enterprises. These agencies are likely to resist streamlining the regulation, which will transfer control over the insurance money from them to new supervisory body.

The main argument to win allegiance of these governmental bodies is the fact that opening of the market is related only to non-government insurance. All of these stakeholders will retain control over the flow of the budget moneys allocated for government needs.

Recommendation

In order to achieve the following goals:

- Formulate a new negotiation position that will allow foreign companies access to the previously closed non-state mandatory insurance sector.
- Formulate new laws and policies in the sector of mandatory insurance that further clarifies the rules for mandatory insurance market.
- Formulate advanced regulatory/supervisory mechanism for insurance sector (representing a combination of state supervision/regulation and limited self-regulation by the independent federal insurance industry association).

It is recommended that the Ministry of Economic Development and Trade creates a coalition of likeminded organizations and government agencies to implement a reform in regulation and rules of foreign companies' access to the non-state mandatory insurance market. The recommended reform will encompass adoption of new legislation:

- On Insurance – the new law will exclude the present limitation of foreign ownership in the insurance companies operating under mandatory insurance licenses.
- On Insurance Regulation and Supervision – the new law will streamline the regulation and will include the provision on possibilities of separating the regulatory functions between the government supervisor/regulator and independent federal regulatory body
- On Mandatory Insurance – the law will reinforce the mechanism of unified or dual regulation specifically in the mandatory insurance sector.

It is recommended that the strategy focus on mandatory (non-state) insurance for the reason that foreign companies desire to effectively participate in the expanding market in the short term. The proposed strategy must be implemented before new law on mandatory automobile insurance comes into effect.

The strategy will allow the Ministry to become one step closer to the conclusion of the WTO negotiation, while advancing the much needed legislative work on creating laws for the fast growing insurance sector.

The WTO accession process is being advanced in two ways:

- Negotiating position will now include market access for the foreign insurers in the mandatory type of insurance

- Part of Insurance Regulation becomes independent, while state regulation becomes more effective.

Strategy:

The proposed strategy sets out an elaborate sequence of events and undertakings necessary to influence the stakeholders and to secure their support. The recommended strategy will achieve the following objectives:

- Create a coalition of like-minded organizations within the executive branch of the Russian government and within the Russian business community.
- Initiate insurance policy reform within the executive branch of the Russian government
- Ensure the adoption of necessary legislation by the Federal Assembly of the Russian Federation
- Changes in insurance regulatory process will advance the WTO accession negotiating process

WTO negotiations:

Reformulate negotiating position to allow for foreign company access to the mandatory insurance market.

Domestic:

0. Generating objective criteria; to support economic rationale behind the proposed reforms order study to the CSR think-tank affiliated with the Ministry of Economic Development and Trade.

Coalition building

1. Win ARIA's support for the project of opening up mandatory insurance market, by

- Supporting their fight for independent self-regulatory status
- Supporting their efforts to streamline the regulation
- Basing on the objective criteria of other markets experiences, demonstrate that market growth will allow everybody to be successful, expansion of foreign presence will not come at the expense of domestic insurers
- Emphasizing that foreigners bring new technologies and WTO accession will enable Russian insurers to more efficiently follow their clients abroad
- Introduce studies done by the CSR think tank

Operational documents and organizational forms of work:

Meetings with ARIA leadership
Signing memorandum of understanding
Joint drafting of appropriate legislation

2. Engage larger business association RUIE. Translate ARIA's support into the RUIE position. Arguments to be presented to the RUIE membership:

- Speedier accession to the WTO
- Ability to bring their own captive insurers to the foreign markets

Operational documents and organizational forms of work:

Meetings with RUIE leadership
Joint letters to the Government officials and the President

3. Building consensus within the government

Once the business community is on board start building consensus within the executive branch that will lead to introduction of the appropriate legislation in the State Duma

3.a. Bring onboard the Finance Ministry by supporting ARIA's lobbying efforts with the ISD in its pursuit to streamline the regulation of mandatory insurance.

Translate ARIA's support for opening of the mandatory insurance market into official ISD position on relaxation of negotiating position for WTO accession.

To follow through on the promise to ARIA to support their fight for SRB status, lobby the ISD and Ministry of Finance as a whole for new regulations of insurance emphasizing the following:

- Improvement of the regulatory process
- Regulation becomes cheaper for ISD
- More efficient insurance market creates greater tax revenues

Operational documents and organizational forms of work:

Meetings with Finance Minister, ISD leadership
Joint letters from ARIA and RUIE
Popularization of studies done by CSR

3.b. Win Prime Minister's support for inclusion of streamlining the regulation of mandatory insurance in new policy for insurance, relaxation of the WTO negotiating position on mandatory insurance.

Required are joint efforts by the Finance Ministry and the Ministry of Economic Development and Trade, and those of ARIA as well as of RUIE.

Operational documents and organizational forms of work:

Joint letters from the ministries
Joint letters from the business associations
Vocal support at the interagency meetings on the WTO accession process

3.c. Other regulators

Avoid vocal opposition of the mandatory insurance regulation streamlining from the disadvantaged regulators by emphasizing the retained control over the budget money spent on those types of insurance as a form of social security mechanism.

Operational documents and organizational forms of work:

Back room meetings with the regulators emphasizing gains from the more effective regulation

4. President

Gain the President's support by emphasizing technological advantages, market growth and ARIA's, as well RUIE's support.

The President's personal meetings with the board of the RUIE will become the most effective venue for bringing this information to his attention.

Both points of 1) reformulating the negotiation position as well as of 2) the regulatory reform "demanded" by the industry have to be supported by the appropriate conclusions from the Ministry of Finance and the Ministry of Economic Development and Trade supporting the proposal.

Operational documents and organizational forms of work:

Influencing the agenda of RUIE meetings with the President
Joint letters from ARIA and RUIE
Joint letters from Ministries

5. Coalition built along the lines described above will allow us to implement the following **legislative strategy**

The goal of the legislative strategy is to pass all of the following or a sufficient combination of laws on insurance.

Law on Insurance Business
Law on Insurance Supervision and Regulation
Law on Mandatory Insurance

All three components can be submitted as either

Government package of legislation on insurance, or
Government package of legislation implementing the WTO obligations

5.a. In either scenario main legislative lobbying efforts have to be concentrated on the specialized Duma committee: Committee on Credit Institutions and Financial Markets.

ARIA automatically becomes a powerful lobbying ally, since the Insurance subcommittee chair is ARIA's president.

The Closeness of the factional position of the Peoples Deputy Faction to that of Unity Faction guarantees support of the Committee's chair, either current Shokhin or any possible future chair.

The Communist Faction opposition to the expansion of mandatory insurance will have to be neutralized by the following:

Media strategy

“Dear colleague” letters from the specialized committee members.

5.b. Senate

Legislative lobbying in the upper house of the federal assembly will have as its goal: winning support of the specialized committee – Committee on Financial Markets and Money Circulation.

Specifically the following Senate members will have to be lobbied:

Chair: Vasilyev Sergei

First Deputy Chair: Buslova Galina

Deputy Chairs: Petrov Gherman, Fetisov Gleb

Members: Vinogradov, Morozov, Provkin, Tatarinov, Troshin

Operational documents and organizational forms of work:

Meetings with Committee leadership

“Dear colleague” letters

Direct lobbying efforts by the ARIA

Media strategy

Media strategy will have as its goal improvement of insurance culture in Russia, popularization of insurance services, generating an acceptance of mandatory insurance by the populace.

Jointly with ARIA, we will launch a federation-wide media campaign “Insure Your Risks and Sleep Well”. In constructing the media campaign, we will capitalize on the positive experience of the Tax Collection Ministry's campaign “Pay Your Taxes and Sleep Well”

The following news outlets have to be engaged to reach the general public:

TV stations: ORT, RTR, NTV, Ren-TV,

Radio networks: Europa-Plus, Russkoye Radio, Mayak, and Radio Rossii.

Printed Media: Komsomolskaya Pravda, Moskovskii Komsomolets, Trud, etc.

Aside from news outlets outdoor media will be utilized.

Sample Budget for June- August of 2002

CSR Study	\$20,000
As the strategy will be carried out from the main offices of the Ministry of Economic Development and Trade, office expenses will be covered from the operating Budget of the ministry	
Staff	
ARIA communications, 1	\$9,000
RUIE communications, 1	\$9,000
Interagency communications, 2	\$18,000
Total for the Ministry of EDT	\$56,000
Media campaign	
4 TV networks, 5 ads a day, at \$10,000 a piece, for 30 days a month	\$200,000 a day
Total 3 months	\$18 million
4 radio networks, 10 ads a day, at \$1,000 a piece, for 30 days a month	\$40,000 a day
Total 3 months	\$3.6 million
Printed media advertising \$1 million a month	
Total 3 months	\$3 million
Outdoor ads \$1 million a month	
Total 3 months	\$3 million
Total for media campaign (coalition of ARIA, RUIE. others)	\$27.6 million

ANNEX I

STAKEHOLDERS CHART

Stakeholder/position	Interest	Options	Objective Criteria	BATNA	Mobilization ideas
US – Ministry of Economic Development and Trade Minister Gref – part of Putin’s team	<ul style="list-style-type: none"> – Develop policies for insurance market, in accordance with the government’s program – Fulfill the WTO accession mandate – Develop strategies for sustainable economic development 	<ul style="list-style-type: none"> – Adoption of a Packet WTO accession-related laws/ economic reform laws/ insurance reform laws – Formulating licensing/registration procedures 	<ul style="list-style-type: none"> – Foreign experience – Hungary/ China – Benefits of WTO accession – WTO rules 	<ul style="list-style-type: none"> – Status quo – Continue WTO negotiations, while continuing formulating principles of socio-economic policy of Russian government 	

Stakeholder/position	Interest	Options	Objective Criteria	BATNA	Mobilization ideas
Ministry of Finance, insurance supervision department Minister Kudrin – part of Putin’s team	<ul style="list-style-type: none"> – Maintain insurance sector’s manageability and accountability – Efficient regulation – Retain control over growing capital flows in insurance sector 	<ul style="list-style-type: none"> – New legislation on insurance regulation and supervision, that secures better financing for state regulators and establishes independent regulator – Approve the creation of self-regulatory body, limiting the right of such body 	<ul style="list-style-type: none"> – Current legislation that they have to enforce – Successful practice of past years – Foreign experience 	<ul style="list-style-type: none"> – Status quo 	<ul style="list-style-type: none"> – Growth of tax base – More efficient use of budget resources – More efficient methods of collecting and analyzing the sector information

Stakeholder/position	Interest	Options	Objective Criteria	BATNA	Mobilization ideas
The President Putin – elected in 2000	<ul style="list-style-type: none"> – Reelection 2004 – WTO accession (symbolizes foreign policy success – recognition of Russia as a market economy) – Development of Russian Insurance market – Avoid political liabilities in front of domestic insurers/populace 	<ul style="list-style-type: none"> – Appoint new ministers – Give in to protectionists pressures – Apply his political clout to pass through the Duma liberal legislation 	<ul style="list-style-type: none"> – Same as the Economy Ministry, since the ministry is operating under his mandate for setting policies and negotiating for WTO accession 	<ul style="list-style-type: none"> – Status quo 	<ul style="list-style-type: none"> – Provide lobbying tools for effective liberalization campaign – Growth of tax base

Stakeholder/position	Interest	Options	Objective Criteria	BATNA	Mobilization ideas
Russian Insurers, represented by All-Russian Insurance Association - ARIA	<ul style="list-style-type: none"> - Protect underdeveloped domestic industry - Become self-regulatory body for Russian insurance sector - Develop legal framework for insurance - Avoid unnecessary government control - Access to foreign markets (both acquiring new business and following current clients in overseas markets) - Transfer of technology 	<ul style="list-style-type: none"> - Lobby – Economy, Finance ministries, President’s administration to preserve current protectionist regime in insurance market - Cooperation with Russian Union of Manufacturers and Industrialists - Lobby individual Duma Members 	<ul style="list-style-type: none"> - Negative Foreign experience (lack of technological gains, lost market share) - Lack of technologies/capital - Cumbersome current state regulation/supervision - 	-	<ul style="list-style-type: none"> - Provide support for Self-regulatory status - Smaller share of a larger pie (after foreigner gain access to Russian market) – still attractive - Invite to draft the appropriate legislation - Access to foreign markets - Technological gains

Stakeholder/position	Interest	Options	Objective Criteria	BATNA	Mobilization ideas
Russian Populace	<ul style="list-style-type: none"> – Better functioning insurance market – Lower premiums – Avoid “new taxes”, skewed perception of mandatory insurance, especially remittance of premiums to foreigners 	<ul style="list-style-type: none"> – Vote 	<ul style="list-style-type: none"> – Current costs to the economy of low insurance penetration – Greater stability due to expanded coverage 	<ul style="list-style-type: none"> – Status quo 	<ul style="list-style-type: none"> – Insurance education campaign – WTO benefits education campaign (fits into a bigger strategy)
The Sate Duma factions					
Unity fraction (80 deputies)	<ul style="list-style-type: none"> – Support the President’s and government’s position 	<ul style="list-style-type: none"> – Support legislation introduced by the Ministry and ARIA – Build on the strong relationship with the Kremlin 	<ul style="list-style-type: none"> – Same as for the Ministry of EDT 	<ul style="list-style-type: none"> – 	<ul style="list-style-type: none"> – Submission of insurance laws/economic reform package – Insurance education – Market expansion –

Stakeholder/position	Interest	Options	Objective Criteria	BATNA	Mobilization ideas
Communist Party (85 deputies)	<ul style="list-style-type: none"> – Opposition to the President – Avoid additional taxation, as mandatory insurance is perceived as such, let alone let the foreigners participate in such collections 	<ul style="list-style-type: none"> – Block necessary legislation 	<ul style="list-style-type: none"> – Poor acceptance of mandatory insurance by general populace 	<ul style="list-style-type: none"> – Boycott 	<ul style="list-style-type: none"> – Popularization of insurance – Media campaign
FOREIGN					
AIG Allianz AG	<ul style="list-style-type: none"> – Market expansion – Protection of earlier investments – More efficient regulation 	<ul style="list-style-type: none"> – Lobby respective governments – Lobby ministries/Duma within Russia – Influence the decisions in the ARIA 	<ul style="list-style-type: none"> – Technological transfers – Previous experience in independent self-regulation 	<ul style="list-style-type: none"> – Status quo – working under the grandfathering rules of current legislation 	<ul style="list-style-type: none"> – Very self-mobilizing group
Foreign Governments – WTO working group partners: US EU Japan Switzerland	<ul style="list-style-type: none"> – Admit Russia into WTO on conditions favorable for their constituents 	<ul style="list-style-type: none"> – Offer technical assistance in insurance regulation – 	<ul style="list-style-type: none"> – WTO rules – Extensive regulation experience 	<ul style="list-style-type: none"> – Not approving Russia’s WTO membership 	<ul style="list-style-type: none"> –

ANNEX II / Dear Colleague Letter

TO HONORABLE DEPUTIES
OF THE STATE DUMA
OF THE FEDERAL ASSEMBLY
OF THE RUSSIAN FEDERATION

Dear colleague,

Russia is poised to expand its fast growing and very important to the economy insurance market. Insurance sector plays the following key roles in the economy: providing economic stability for the enterprises and populace in cases of emergency and accumulating investment capital for development of business projects.

Expansion of insurance market in Russia is closely tied with Russia's accession to the World Trade Organization. The Government of Russia has come up with a creative solution on how to satisfy requests of the WTO counterparts while protecting interests of the domestic insurance market and ensuring its growth. It is a multifaceted solution, however the main thrust of the strategy is allowing greater foreign access to the Russian mandatory insurance market.

Not only the Russian mandatory insurance market is underdeveloped, its regulation is drastically lagging behind the modern regulatory practices. The other prong of the solution foresees streamlining the insurance regulatory process. Many sectors of the economy lack efficient and effective regulation. We need to take affirmative steps to improving regulatory environment in all sectors. Insurance lends itself as an excellent starting point to commence such a reform.

Such a combination of liberalization of mandatory insurance and insurance regulatory reform secures wide industry support for the reform, liberalization of the market, and for allowing more foreign access to the market. Not only expansion of mandatory insurance will benefit the economy through increased stability in different sectors of the economy; but its liberalization, more foreign access will bring new capital, new efficiencies and know-how to the entire insurance sector.

For these reasons I urge you to support the Insurance Legislative Package submitted by the Ministry of Economic Development and Trade.

Sincerely,

Alexander Koval'
Chair
Insurance Subcommittee
State Duma of the Russian Federation

ANNEX III / MEDIA RELEASE

RUSSIAN FEDERATION

MINISTRY OF ECONOMIC DEVELOPMENT AND TRADE

FOR IMMEDIATE RELEASE

May 11, 2002

CONTACT

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Ministry and Industrial Association Launch a Campaign
“Insure and Sleep Well”

Minister of Economic Development and Trade G. Gref and President of the All-Russian Insurance Association A. Koval’ commence federal campaign to promote insurance in Russia at press conference on May 11, 2002

MOSCOW, May 11 -- Press conference on new media campaign to promote insurance will be held at 10.00 am at the Ministry of Economic Development and Trade on May 11, 2002 in Moscow.

Both the Ministry and All-Russian Insurance Association agreed to launch a joint campaign to popularize insurance in Russia. The goal of the campaign is to overcome resistance of the general public to mandatory insurance in light of approaching entry into force of the mandatory auto-insurance law. This law alone will increase the Russian insurance market by \$1 billion. As in many foreign states, mandatory auto-insurance law is intended to increase stability and mitigate losses arising from numerous road accidents. However, public and some factions in the State Duma, such as Communist Party, perceive mandatory insurance as another form of tax on auto-owners.

The designers of campaign also want to promote insurance sector as a whole, and not only the mandatory insurance sector. Russian economy is underinsured: insurance penetration ratio, currently at 2.5% of GDP, is lagging behind other transitional economies by a factor of two, and behind the OECD countries by a factor of four. Russian Insurance Association estimates that insurance sector alone is capable of adding .3-.4 % annually to GDP growth.

Campaign budget is estimated at roughly \$10 million every month and the monetary resources are to be provided by the Russian insurance industry.

More information is available on the websites of the Ministry of Economic Development and Trade and of the Insurance association: www.economy.gov.ru and www.ins-union.ru

ANNEX IV / Briefing Memorandum

TO: HONORABLE GHERMAN GREF, MINISTER OF ECONOMIC
DEVELOPMENT AND TRADE OF THE RUSSIAN FEDERATION
FROM: TIMOUR KARIMOV, CONSULTANT
DATE: APRIL 5, 2002
RE: RUSSIA'S WTO ACCESSION INSURANCE

ISSUE

The Russian Federal Law on Insurance (1999) prohibits the sale of life and mandatory/compulsory types of insurance by majority foreign owned (>49%) insurers. Foreign participants in the insurance sector are unsatisfied with the level of protection for domestic companies. According to the Law, foreign insurers cannot make investments that would provide control over their Russian subsidiaries without losing mandatory and life insurance licenses. This issue inhibits Russia's WTO accession process.

RECOMMENDATION

It is recommended that the Ministry of Economic Development and Trade of the Russian Federation initiates a reformulation of Russia's WTO accession negotiating position with the view of allowing foreign companies' access to the domestic non-state mandatory insurance market.

Such a reformulation, conducted in accordance with the proposed strategy, will help the Russian negotiating team move forward accession talks with their WTO counterparts, while advancing the much needed modernization of insurance related policies and domestic legislation.

The recommended timeframe for the implementation of the proposed strategy is 2002 through the first half of 2003. At the end of this period, Russian Federation legislation on mandatory automobile owners liability insurance takes effect. This legislation alone will expand the Russian insurance market by \$1 billion. The ability of foreign investors to participate in such a large sector of the insurance market guarantees their active support for this proposal and guarantees more effective transfer of new technologies.

Benefits to the National Economy

Foreign companies' access to the Russian insurance market benefits the national economy in the following ways:

- Inflow of additional capital to the insurance sector;
- Transfer of advanced technology, experience, and education; and
- Introduction of price competition.

The widely held belief that foreign companies' access to the Russian insurance market will significantly increase outflow of the capital is disproved by examples in other transition economies. The protection of the domestic insurance market does not solve the problem of capital outflow from the country. Domestic insurance companies equally contribute to the capital outflow through reinsurance and placement of investments abroad. Further elaboration of legislation regulating placement of capital and reinsurance abroad is necessary to address the issue of capital outflow.

PROPOSED STRATEGY

In order to reformulate the WTO accession negotiating position on insurance and to amend existing discriminatory insurance legislation it is recommended that the Ministry builds a coalition that includes the following: the All-Russian Insurance Association (ARIA), the Russian Union of Industrialists and Entrepreneurs (RUIE), the Ministry of Finance, the Prime Minister, and the President.

The Ministry's support for ARIA's strive to become an independent self-regulatory body as well as the explicit intent of the proposed reforms to streamline the insurance regulation will guarantee ARIA's cooperation. With respect to the matter of the proposed reform RUIE's membership is interested in speedier accession to the WTO and in being able to bring their own captive insurance companies to the foreign markets. Considering the relationship between ARIA and RUIE, ARIA's support for reform support of RUIE. The business community's backing for this proposal facilitates the further strengthening of the coalition by engaging the Prime Minister and the President.

A coalition built along the lines described above will make possible the implementation of the LEGISLATIVE STRATEGY, that will secure foreign access to the Russian non-state mandatory insurance market. The strategy will ensure passage through the Federal Assembly of sufficient combination of insurance legislations: a) Law on Insurance; b) Law on Insurance Supervision and Regulation; and c) Law on Mandatory Insurance.