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Insurance and risk management systems in Russia¹

*Nadezda Kirillova*²

Abstract: The article presents the results of a study of Russian insurance risk management systems. In particular it covers issues related to corporate insurance in the Russian Federation, the method of formation of corporate insurance systems, financial condition assessment tools for insurers and insurance service users and a recommendation for improvements to the insurance enterprise systems in the Russian Federation. This study offers a summary statistical data on the insurance market.

Keywords: insurance, risk management, Russian Federation, technical risk, financial stability, policyholder protection.

JEL codes: K43.

Introduction

An open competitive environment is a requisite for the improvement in productivity, an increase in private investment activity and support of the national economy. Insurance plays an important role in this regard. Insurance is also one of the most efficient, stable and clear mechanisms in managing risks arising from businesses with different needs. The benefit of insurance can be found throughout the last 20 years of capital market development in the Russian Federation. Currently risk management, including risk financing through insurance, of large industrial complexes is no longer just to manage individual risks one at a time but to manage all of them with a built-in, integrated risk management system.

For the development of financially and operationally sound insurance systems we need a transparent infrastructure within the systems. This includes but is not limited to a definition and differentiation of insurable risks, identification of risk retention processes, creation of a private insurance system, definition of insurance companies and the proper evaluation of their financial con-

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ditions. Standardization of the insurance systems, markets, insurers and other critical elements is thus required. This study attempts to address these issues.

The article focuses on the organization of corporate insurance in the Russian Federation. The paper is organized as follows. Section 1 describes the general characteristics of corporate insurance in Russia. Section 2 presents the methodology of formation and functioning of corporate insurance programmes. Another part is devoted to the identification of the financial condition of insurers (Section 3). The author's conclusions and a systematization of corporate insurance systems are shown in Section 4 and are based on the current data and the real experiences of modern corporate industrial insurers.

1. Corporate Insurance in the Russian insurance system

The modern private insurance system in Russia can be said to have developed with the adoption of the new law of Insurance in 1992 (or a little earlier with the appearance of the first insurance cooperatives). Historically the driver of this development has been corporate and mostly industrial structure-related. This trend still continues. The consumption of insurance in the 1990's was, however, often through cases of so-called "grey schemes," created for the for minimization of income tax liabilities (and encashment in times of crisis). Then came insurance contracts initiated by banks as part of their process of granting loans, as were insurance contracts for foreign partners in international projects.

Insurance on property risks as well as (quasi-) social insurance for employees (for example, packages for voluntary accident insurance and voluntary health insurance) began to form in Russia. This reflects the development of a meaningful insurance system, thus protecting consumers in general against the negative consequences of various risks. The share of property insurance – in terms of premiums and mainly for legal entities amounted to 393,82 billion roubles or 43,5% of the total insurance premiums in 2013, and to 420.4 billion roubles or 42.6% of the total insurance premiums in 2014 [The Central Bank 2015]. In 2012 the total volume of property insurance premiums insurance of legal entities amounted to 57% of the market [Federal], see Table 1 and 2 for a summary of data for 2013 and 2014.

2. Methods of corporate insurance programmes

A comprehensive insurance coverage for the corporate insured involves the following procedures:

- detection of risks and identification of insurable risks;
- integrated approaches for the assessment of insurable risks;

Table 1. Premiums and Claims payments in the Russian Federation 2013

Type of insurance	Premiums				Claims			
	Bln. r.	Bln. EUR	% of total	% (the previous year)	Bln. r.	Bln. EUR	% of total	% (the previous year)
Life insurance	84.89	1.9	9.4	160.5	12.33	0.3	2.9	92.4
Personal insurance (non-life)	208.73	4.6	23.1	113.2	103.14	2.3	24.5	110.9
Property insurance	393.82	8.8	43.5	104.6	201.73	4.5	48.0	111.0
Liability insurance	29.74	0.7	3.3	99.4	7.14	0.2	1.7	133.0
Business and financial risks	21.95	0.5	2.4	110.2	1.66	0.04	0.4	79.4
Total voluntary insurance	739.13	16.4	81.7	111.4	326.0	7.2	77.5	110.3
Compulsory insurance of civil liability for motor vehicle owners	134.25	3.0	14.8	110.3	77.37	1.7	18.4	119.0
Other than medical and motorcycle	31.48	0.7	3.5	109.4	17.4	0.4	4.1	144.9
Total compulsory	165.73	3.7	18.3	110.2	94.77	2.1	22.5	123.1
Total voluntary and compulsory	904.86	20.1	100.0	111.1	420.77	9.4	100.0	112.9

Currency rate as at 01.01.2014: 1 euro = 45 roubles.

Source: <http://www.cbr.ru>.

Table 2. Premiums and Claims payments in the Russian Federation 2014

Type of insurance	Premiums			Claims			
	Bln. r.	Bln. EUR	% (the previous year)	Bln. r.	Bln. EUR	% of total	% (the previous year)
Life insurance	108.53	1.6	11.0	14.23	0.21	3.0	115.3
Personal insurance (non-life)	219.58	3.23	22.2	110.49	1.62	23.4	106.5
Property insurance	420.4	6.18	42.6	224.51	3.3	47.5	110.3
Liability insurance	37.85	0.56	3.8	10.3	0.15	2.2	142.9
Business and financial risks	22.56	0.33	2.3	3.54	0.05	0.8	208.2
Total voluntary insurance	808.92	11.9	81.9	363.07	5.34	76.9	110.5
Compulsory insurance of civil liability for motor vehicle owners	150.92	2.22	15.3	90.31	1.33	19.1	116.0
Other than medical and motorcycle	27.93	0.41	2.8	18.89	0.28	4.0	108.5
Total compulsory	178.85	2.63	18.1	109.2	1.61	23.1	114.6
Total voluntary and compulsory	987.77	14.53	100.0	472.27	6.28	100.0	111.4

Currency rate as at 01.01.2015: 1 euro = 68 roubles.

Source: <http://www.cbr.ru>.

- development of a methodology of forming and using risk maps of industrial and financial risks, liability risks, personal risk;
 - self-evaluation of relations and security; estimation of insurance costs and the economic effect;
 - creating technical specifications of insurance cover;
 - examination of the financial condition of insurers – contractors insurance programmes;
- monitoring and evaluation of insurance programmes from the standpoint of industrial insurers, as illustrated in Figure 1.

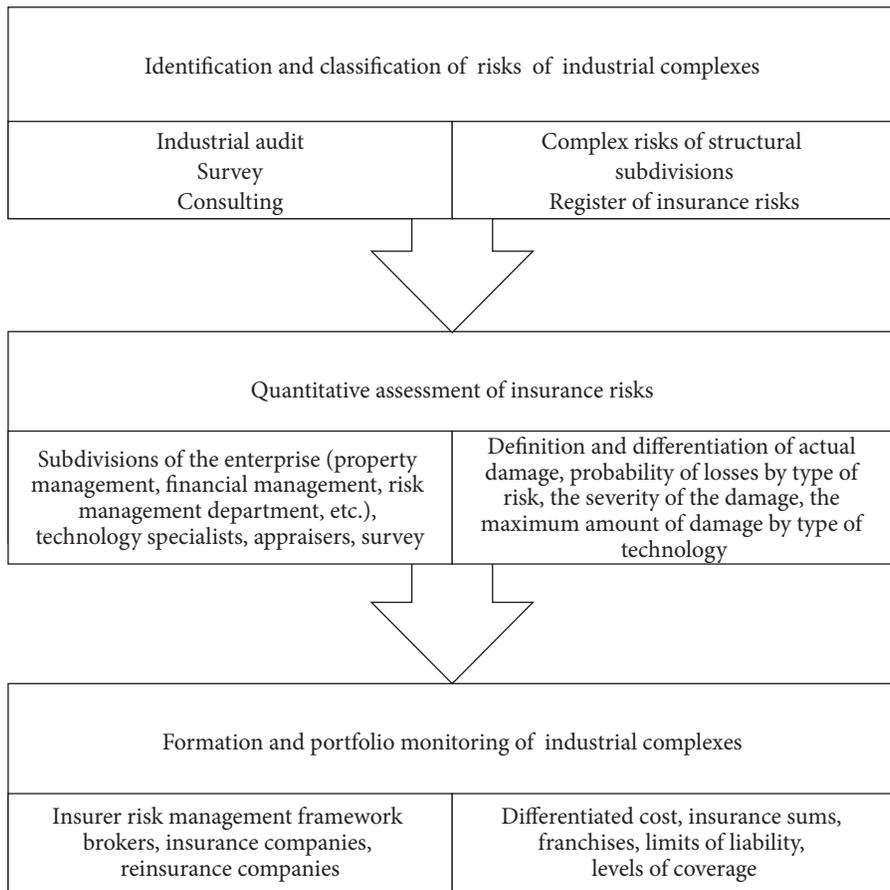


Figure 1. Formation of an insurance system industrial complex

Key elements in the formation of insurance programmes are:

- the limits of liability insurance;
- availability of reinsurance cover;
- the assessment self-insurance – determination of the size of franchises.

The search for optimal mechanisms to increase the working capital and capital reinvestment requirements lead to the use of new mechanisms for interaction with insurers, reinsurers and reinsurance brokers; requirements cover industrial risks, risks which encourage staff to create captive insurance companies to enter the international reinsurance market, to optimize the methods for identifying and the evaluation of the financial state of insurance companies, Figure 2 [Kirillova 2007, 2008].

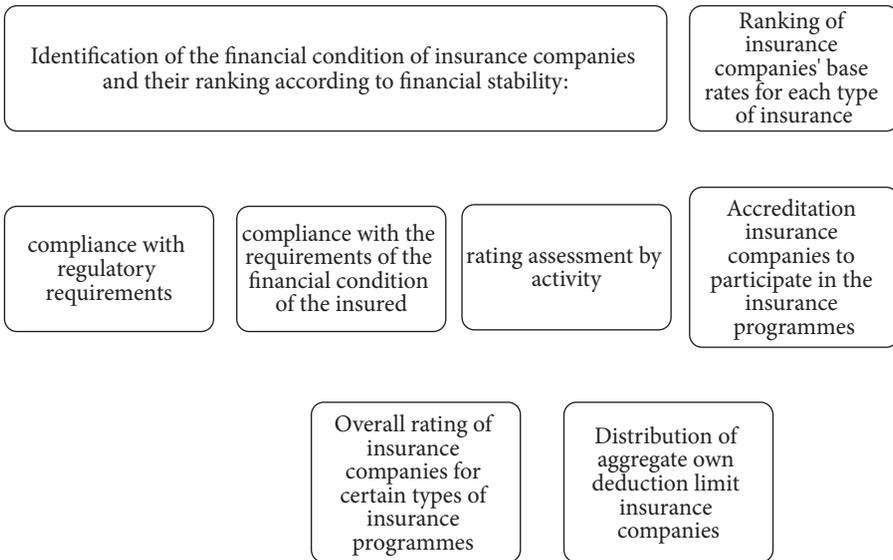


Figure 2. Distribution of the aggregate limit of own deduction of insurance companies in the insurance programmes

3. Identification of the financial condition of insurance companies

In accordance with Russian legislation the guarantees of the financial stability of the insurer are:

- economically reasonable insurance tariffs;
- insurance reserves, sufficient for the fulfillment of obligations under contracts of insurance, coinsurance, reinsurance, mutual insurance;
- equity;
- reinsurance (minimum capital for Russian companies 120 million roubles on insurance other than life; 240 million roubles for life insurance and 480 million roubles for reinsurance); formation and placement of insurance reserves, covering equity assets.

Legislation also defines the basic requirements of the financial condition of insurers:

- solvency margin;
- placement of insurance reserves;
- assets covering equity;
- net assets (for joint stock companies).

Along with the regulatory requirements for the financial condition of insurers those insured made their demands.

Significant factors in optimal insurance protection can be combined in the following areas:

- history of the insurance company relationships with the company;
- management of the insurance company and its business reputation in the insurance market;
- tariff policy, the promotion and adaptation of insurance products;
- reinsurance;
- financial condition of insurers (set of economic indicators) – Figure 3.

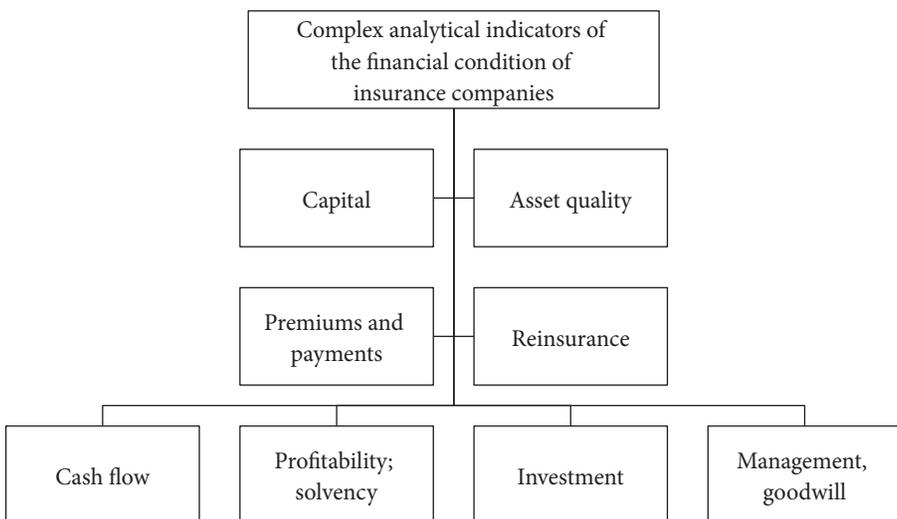


Figure 3. The main directions of financial state evaluation of insurance companies

If all the legislative requirements are normal, the performance analysis unit can be assessed in four areas:

- insurance,
- reinsurance,
- investment,
- management and goodwill of the insurer.

4. Modern approaches to the formation of corporate insurance systems in the Russian Federation

Currently corporate systems of industrial enterprises in Russia are developing very differently. A description of integrated approaches to the formation of risk management systems with an insurance basis and separate requirements for property insurance in respect of mortgages can easily be identified.

For example, Magnitogorsk Iron and Steel Works was amongst the first in the steel industry to have developed and implemented a comprehensive risk management system: a risk management division, an approved risk management policy and a corporate standard for risk management.

In the annual report the following risk management policy is stated:

- identification and evaluation of the principal risks faced by MMK group;
- completion of the introduction of a comprehensive risk management system;
- introduction of a multi-faceted approach to the evaluation of risks of building and structural failure;
- improvement of risk management procedures regarding non-fulfilment of payment obligations for steel products;
- to mitigate the risk of production stoppages, the CEO approved the list of plants considered production bottlenecks [OJSC].

In another big energy company, Rosseti, along with compulsory health insurance and compulsory insurance against accidents at work, the company declared support and development of additional corporate voluntary medical insurance, voluntary insurance against accidents and illnesses, private pension provision [Rosseti]. In the consolidated annual accounts it is indicated that the group did not have full coverage for its plant facilities, business interruption, or any third party liability in respect of damage caused to the estate or the environment as a result of accidents or for the Group. As long as the Group obtains adequate insurance coverage, there is a risk that the loss or destruction of certain assets could have a materially adverse effect on the financial position of the Group.

In the requirements for the head of risk management Irkutsk Oil Company stated following:

- development of risk management methodology (concepts, risk management policy, risk and specifications, etc.);
- planning for the creation of risk management systems and the achievement of the stated objectives of risk management;
- carrying out purposeful work to identify threats of loss and to identify the sources of risk (analysis reporting, business audits and audit, analysis of management decisions, analysis of the causes of deviations, etc.);
- risk assessment, quality and effectiveness of the existing risk management system;

- establishing and maintaining up to date risk maps for each of these risks;
 - software development, coordination and organization of goals set for the detailed risk, being in the responsibility of risk managers and owners;
 - ensuring the implementation and application of the necessary organizational and managerial forms of work to achieve the objectives of risk management in their area of responsibility, and the active integration in their work;
 - control of the accuracy, adequacy or completeness of the approved control procedures and risk management;
 - advising on business process optimization and improvement of economic activity of the internal control of the Company and subsidiaries and affiliates;
 - controlling the goals enshrined in risk retention within the prescribed limits.
 - conducting periodic reporting on the effectiveness of risk management in its area of responsibility for the management unit and the company;
- logging of data related to sales and any potential risks in their area of responsibility: [OOO Irkutsk].

Thus we see that the understanding of the necessity and value of insurance arises from different sources. Nevertheless there is no common approach as the methodological base is so diverse that it creates certain difficulties in the formation and development of systems for insurance enterprises.

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Aims and Scope

Economics and Business Review is the successor to the Poznań University of Economics Review which was published by the Poznań University of Economics Press in 2001–2014. The Economics and Business Review is a quarterly journal focusing on theoretical and applied research work in the fields of economics, management and finance. The Review welcomes the submission of articles for publication dealing with micro, mezzo and macro issues. All texts are double-blind assessed by independent reviewers prior to acceptance.

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