CONTENTS

Overview of the Themes

This special issue brings to you the editorial and eleven articles, which highlight three segments: insurance undertakings in transition countries, Slovenian insurers at the entry point to the European Union, and a cross-section of experience gained by insurers in special areas of the industry.

The editorial written by *Mirko Kaluža*, the director of the Slovenian Insurance Association, paints the actual moment of the local insurance industry when Slovenia joins the club, balancing optimistic expectations and a feeling of wariness experienced by the insurance industry.

The first part addresses insurance wrapped up with banking (bankassurance) in transition countries. *Franjo Štiblar* and *Filip Šramel* review the legislative framework for insurance undertakings in ten new Member States at the accession to the EU as the platform for assessing chances for a foothold in their insurance markets. A broader view of bankassurance as a "hot" financial product is presented by *Marjan Kramar* and *Miran Vičič* who on the case of NLB, the biggest Slovenian bank, show pros and cons for bankassurance. *Franjo Štiblar* is the author of an in-depth empirical analysis of the insurance markets of new Member States on the eve of the EU accession in comparison with EU-15, and focuses on the bill of health of the Slovenian insurance industry.

The second part of the special issue of Bančni vestnik (Banking yournal) looks into the position of the Slovenian insurers in the EU. First, *Jurij Gorišek* provides an exhaustive account of the preparations of the Slovenian insurance industry for the EU from the supervisory authority's angle. Then *Siniša Lovrinčević* describes the challenges faced by the Slovenian reinsurance industry in the light of the importance that reinsurance enjoys worldwide.

Past experience shared by the Slovenian insurance undertakings is the content of the third part with actions taken in particular insurance segments. *Andrej Kocič* opens the discussion by describing financing of natural catastrophes around the globe, with Slovenia under the looking glass. The theoretical aspect of risk underwriting and claims support of life assurance is elaborated by *Darko Medved.* The specific features of supplementary insurance in place in Slovenia are examined by *Helena Bešter* (supplementary retirement provision) and *Marko Jaklič* (voluntary heath insurance). *Edi Glavič* provides a comparative analysis of the comprehensive automobile insurance in the neighbouring Austria and Italy, and in Slovenia. How credit insurance is arranged by the Slovenian Export Corporation is described by *Bojan Pecher.*

This special issue of Bančni vestnik offering a survey of insurance is a pioneering effort in Slovenia, and aims to provide a comprehensive picture of this segment of Slovenia's financial sector. As already customary for special issues, they are simultaneously published in the Slovenian and the English language. So far, only the financial sector in general and the banking industry in particular have been in the mainstream of Bančni vestnik as the challenges associated with the full-fledged EU membership came to the forefront. As the architects of this special issue, we acknowledge that it is a broad-brush approach to insurance-related topics and as such far from being exhaustive. However, it brings insurance in focus and helps to understand its state of health as Slovenia joins the EU. Provided we have managed to answer some of the questions our readers ask about insurance in Slovenia, our mission is completed.

Franjo Štiblar
Advising editor of the Special Issue

Slovenian Insurance Undertakings at the Cross-Roads

*Mirko Kaluža**

The Slovenian insurance market opened up completely as of 1 May, and so it became a tiny piece of the European insurance market. European insurance undertakings have the possibility to sell their insurance freely in Slovenia without setting up branches or other formal organisational forms, and the same possibility is available to Slovenian insurers who are considering selling insurance in the European Member States. It is by no means a small change for domestic insurance undertakings that used to do most business on the protected "home turf". They can think of it as a true challenge to expand the area in which they operate, or as a menace as new providers of insurance services enter the race for a slice of the Slovenian market.

The conditions likely to attract new entrants to the Slovenian insurance market encompass in the first place the following: a highly developed insurance culture coupled with a mature environment which enables a higher degree of offer acceptance and a higher penetration rate; the small portion of life assurance in total gross premium (20 per cent) translates into a substantial market potential; the lack a comprehensive offer in certain insurance segments and in liability insurance in particular; fast-developing insurance infrastructure (agents and brokers) which may significantly facilitate the entry into the Slovenian insurance market. Last but not the least, Slovenia could also be a springboard to the markets of South Eastern Europe.

Among the reasons indicating that no revolutionary changes are to be expected shortly in the Slovenian insurance market, the following might be decisive: the grip on the insurance market is relatively strong with a spate of insurance undertakings whose number is still increasing as banks spread their intermediation into insurance products and services diminishing space for new entrants; general orientation of policyholders to local insurance providers revealed also by European experience so far; comparatively low domestic insurance prices which makes the insurance business less attractive to new providers, and the still unconsolidated ownership situation in the insurance

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industry. As events unfold, it will become clearer whether these assessments have been realistic, as forecasting future development in the Slovenian insurance market is an extremely delicate task made even more difficult in the light of the fact that Slovenia is practically the only country among the new Member States which still has insurance companies controlled by domestic capital.

At the end of the day the most important question to ask is how well have the Slovenian insurance companies done their homework in an effort to prepare for the new situation.

Slovenian insurance undertakings have been relatively successful in exploiting the environment being protected so far in order to prosper. Their operating results have earned them an important place in the economic environment. It is well illustrated by a 5 per cent share of annual gross premiums in GDP (insurance penetration), the average premium per capita (insurance density) amounts to 500 euros, no insurance company has gone bust so far, technical provisions and regulatory own funds meet the effective statutory requirements for solvency. Furthermore, the number of employees in the insurance industry has increased to over 5,500. A number of independent agencies and brokerage houses have been set up to facilitate access to insurance products, the educational structure of people working in insurance has been improving, etc. We can be satisfied with these trends without slipping into complacency. Giving the thumbs up to the insurance industry without voicing some concerns would be superficial. The main feature of the Slovenian insurance market is the domination of composite insurers managing portfolios of different sizes, and regrettably incurring management costs which vary vastly and which at times affects their financial effectiveness. There is a balance to be struck in the area of productivity measured by the average volume of premium per employee, which is still below the level achieved in the developed Europe. It is our estimation that for a composite insurer endowed with the attributes desired if it is to be successful in the Central European market, the annual volume of premium has to be 500 million euros. For the time being, there is just one Slovenian insurance company closing on that benchmark. History teaches us the pressure of competitors will spur the owners of insurance undertakings to close some long-standing deals on integration and concentration. Such concentrations would surely boost competitiveness in the Slovenian market and will throw weight behind the key players competing under newly forged circumstances.

On the other hand, “big” Slovenian insurance companies are contemplating expanding business by entering the markets of neighbouring European countries, and the countries of South-Eastern Europe as a way to win over new clients. They have accepted the challenge posed by the new environment and it is highly probable that they will be successful in beating the odds.

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Regulatory Framework for the Insurance Sector in New EU Member States

*Franjo Štiblar and Filip Šramel**

REGULATORY FRAMEWORK FOR THE INSURANCE SECTOR IN NEW EU MEMBER STATES

This article analyses the regulatory framework dealing with the liberalization of entrance into the insurance market in the 10 new EU member states (statutory law). Special attention is given to solutions adopted in Slovenia compared to other EU old and new member countries. Despite the obligatorty adoption of the acquis, there are certain diffferences between new EU members stemming either from a lack of regulation of certain fields by the EU insurance directives or due to a transition period given to certain countries in adoption of directives. Slovenia adopted a solution similar to most of the new EU Member States in some fields of regulation dealing with the qualifying holdings of ownership, permitted institutional forms of insurance companies (stock holding company and mutual association) and the usual corporate governance bodies (assembly, management board, supervisory board). In other fields Slovenia's regulation is specific, as for instance regarding the discretionary period to answer an application for establishment of an insurance company, a special insurance sector supervisory body, authorisation for composites to continue operating, higher than average requirements for establishment and guaranteed capital, the above average types of technical reservations for insurance companies required as well as in regard to the qualification requirements for members of a management board

In May 2004 Slovenia became a member of the EU-25 together with nine other accession countries. Similarly to other areas, the *acquis communautaire* was adopted for the insurance sector and the country entered the enlarged competitive EU internal market. What kind of conditions can Slovenia expect in comparison to other new members? What are the opportunities to enter insurance markets of other accession countries? What are the prosepects for foreign insurance companies to enter the Slovenian market or for Slovene insurance companies to enter the markets of other EU newcomers?

This article has a goal to find answers to the above and similar questions. In comparative fashion it analyses the main features of regulatory framework in the new EU Member States. There is a threefold comparison: among the new EU Member States themselves, in relation to standards of the EU as defined by the EU insurance directives and other secondary legislation acts, and Slovenia's regulations are comparable to both new and old EU Member States.

The EU insurance directives and other secondary legislation acts create conditions for a genuine internal insurance market of the EU. They cover economic regulation (liberalization and deregulation measures), financial regulation (supervising insurance undertakings to protect the insured and the financial system as a whole) and legal regulation (covering the contractual relationship between insurers and insureds as part of the general consumer protection policy; Labilloy, 2004). The first two areas of statutory

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law are the subject of this paper. It is of special interest to discuss the opportunities to enter insurance markets of the new EU Member States. In a wider sense its subject is the regulation of corporate governance of insurance companies in these countries.

Within the financial system the insurance sector is less strictly regulated and is lagging behind regulation of the banking sector in adopting directives and other EU legislative acts. For regulation of reinsurance companies, for instance, only a proposed solution exits, while in the meantime analogy from regulation of insurance companies is used for them. It is therefore not a surprise that despite the adoption of the acquis, significant differences remain among new EU members in regulation of those areas not regulated by the existing insurance directives.[1]

After the introductory chapter the article analyses individual areas of instituitional regulation (corporate governance) of insurance companies in the logical order of, first, their establishment and, second, running their business. First, the provisions on the procedure of establishing an insurance company are tackled together with their M&A, followed by the representation of the supervisory authority deciding upon these questions. Next, statutory forms which are allowed for insurance companies are described, followed by the presentation of minimum capital requirements (initial or share capital and guarantee fund and forms of technical reserves which insurance companies must create). At the end, provisions on bodies required for insurance undertakings and on qualifications required for their board members are discussed and compared, both being of utmost importance for good corporate governance of insurance undertakings.

In the tables presented in this paper, only the major characteristics of institutional regulation of the insurance sector are compared according to the laws newly adopted by the new EU entrants.[2] It was impossible to analyse all the provisions for the purpose of this comparative study and even the tackled provisions have to be analysed in a simplified form for the sake of comparative transparency.

The insurance sector of the new EU Member States could be divided into three groups defined by the spread of insurance culture and by institutional regulation (Baur, SwissRe, December 2002). First, Malta and Cyprus are already acting in the field of insurance in a similar manner to »old« EU members, only their size does not allow for a major impact in the enlarged EU. Second, the three Baltic states are lagging behind, as they were dependant for a long time on the volatile Russian market. Introduction of compulsory motor insurance and a revival of the Russian economy in 2001 helped in developing their insurance business. Low premiums and increased liberalization indicate good development potential after these countries enter the EU. Third, the remaining five accession countries from Central Europe are potentially the most important for insurance development; with liberalization and consolidation the final outcome is domination of foreign insurance companies. Slovenia has a specific position among them with relatively most developed insurance activity, a smaller share of foreign ownership and the prospect to penetrate insurance markets of other new EU members as well as other East and South-East European countries itself. Slovenia has the highest rated insurance sector among the transition countries by IC EC EU (June 2003).

The Czech Ministry of Finance as the insurance supervisory authority.

REGULATORY FRAMEWORK

The comparative study is based on the most recently (May 2004) adopted insurance laws in EU accession countries and relevant secondary legislation acts dealing with the insurance sector.

In their general provisions all new EU Member States have in their laws introduced the system of single passport and home country control, provisions transposed from the EU insurance (financial) directives. The single passport system means that an insurance company from the EU (in a wider sense from the European Economic Area, EEA) can establish a subsidiary in any EU Member State without special approval from the supervisory authority in the destination country. It is sufficient that there is an announcement of that intention from the home supervisory authority to the host country supervisor.

Insurance companies from the EU (EEA) member states can also execute insurance activities across borders in the framework of free supply of services. Only Estonian law does not explicitly regulate this activity.

On the other hand, insurance companies from third countries can establish subsidiaries in EU Member States only if the host supervisory body gives explicit authorisation for each individual case.

The laws of AC-10 do not define the ownership of insurance companies nor do they limit the ownership share of the largest owner.

Procedure to establish an insurance company

The procedure to obtain authorisation for execution of insurance services is described in the legislation of all analysed countries. The required documentation is given in detail. The provisions about required application documents differ from country to country in some details,

[1] The affirmation of "Societas Europea" will change the situation.

[2] In May 2004 at the time of entry, the EC EU ascertains that the final evaluation of adoption of the acquis by newcomers for the insurance sector can not be made as all newly adopted laws are not yet translated and sent to Brussels. This article goes a step ahead in using the newest information directly from primary sources in each new member country.

Table 1: Issue of insurance license procedure

Country	A time-limit in which insurance supervisor shall hand down a decision	Right to appeal	Reasons for refusal to issue insurance license
Cyprus	6 months	yes	if the conditions listed in the Act are not met
Czech Republic	6 months	not defined in the Act	precisely defined in the Act
Estonia	3 months	yes	defined in the Act, however the Financial Supervision Authority has discretion
Latvia	3 months	yes	precisely defined in the Act
Lithuania	6 months	yes	precisely defined in the Act
Hungary	not defined	not defined in the Act	precisely defined in the Act
Malta	6 months (3 months in case of reinsurance)	yes	if the conditions listed in the Act are not met
Poland	not defined	not defined in the Act	precisely defined in the Act
Slovakia	defined in the special Act	not defined in the Act	if the conditions listed in the Act are not met
Slovenia	not defined	not defined in the Act	precisely defined in the Act

Source: effective legislation of observed countries

but all countries require the following: statutes, business plan and a list of shareholders.

Authorisation to provide insurance services is granted by the supervisory institution. Related laws differ in procedures for issuing authorisation and especially with regard to reasons for rejection of authorisation. The period in which a response to the application should be given starts when the supervisory institution obtains complete application documents. Hungary, Poland and Slovenia do not define the deadline for the supervisory institution to make a decision. In Slovakia, it is set out in a special law. All other new EU members define a 3 or 6 month period for response.

The reasons for rejection of an application are clearly stated in most observed countries. Alternatively, Cyprus, Malta and Slovakia determine that authorisation can be issued if all requirements laid down in the law are fulfilled. Only Estonia in its law gives a discretionary power to the supervisory institution in decision making. Cyprus, Estonia, Latvia, Lituania and Malta permit appeals against the decision of supervisory institution. The laws of other observed countries do not deal with this issue.

ACQUISITION OF QUALIFYING HOLDING

The laws in the new EU Member States define that prior approval of the supervisory institution is needed for obtaining qualifying holding in equity of an insurance company. Only Polish law defines that for a 10% share, a notification to the supervisory institution is sufficient.

Table 2: Qualifying holding

Country	QUALIFYING HOLDING
Cyprus	10%, 20%, 33%, 50%
Czech Republic	10%, 20%, 33%, 50%
Estonia	10%, 20%, 33%, 50%
Latvia	10%, 20%, 33%, 50%
Lithuania	10%, 20%, 33%, 50%
Hungary	10%, 20%, 33%, 50%, 75%
Malta	10%, 20%, 33%, 50%
Poland	10%, 20%, 33%, 50%
Slovakia	10%, 20%, 33%, 50%, 66%
Country	10%, 20%, 33%, 50%

Source: regulatory acts of new EU member countries

In general, the requirement regarding qualifying holding in equity is the same in all new EU Member States, with the threshold being 10%. The ceiling is 50% in all countries except Hungary (75%) and Slovakia (66%).

Supervisory authority

The supervisory institution issues authorisation for taking up insurance services and supervises their business. Cyprus, Lithuania, Poland and Slovenia have special institutions for supervision of insurance companies, while Estonia, Latvia, Hungary, Malta and Slovakia have common supervisory institutions for all financial supervision in one agency. In the Czech Republic supervision is performed directly by the Ministry of Finance.

Composite insurance

No new EU Member State provides for composites in principle. In Slovenia they can remain if they were already in existence at the time of adoption of the new law. As an exception, the life insurance companies are allowed to offer

Table 3: Insurance supervisor

Country	INSURANCE SUPERVISOR
Cyprus	Superintendent of Insurance
Czech Republic	Ministry of Finance
Estonia	Financial Supervision Authority
Latvia	Finance and Capital Market Commission
Lithuania	Insurance Supervisory Commission
Hungary	Hungarian Financial Supervisory Authority
Malta	Malta Financial Services Authority
Poland	Insurance and Pension Funds Supervisory Commission
Slovakia	Financial Market Authority
Slovenia	Insurance Supervision Agency

Source: effective legislation of observed countries

Table 4: Ability to simultaneously carry out life assurance and non-life insurance

Country	YES	NO	NO, with the exception of simultaneously carrying out life assurance and accident and sickness insurance
Cyprus		✓	
Czech Republic			✓
Estonia	✓		
Latvia		✓	
Lithuania			✓
Hungary		✓	
Malta		✓	
Poland		✓	
Slovakia		✓	
Slovenia			✓

Source: effective legislation of observed countries health and accident insurance from the group of non-life insurances in all countries observed, except for Estonia.

Legal forms of insurance undertakings

Most of the new EU Member States recognize two legal forms of insurance undertakings: joint stock companies and mutual associations. Hungary has mutual associations in two forms: insurance cooperative and insurance association. Only in Estonia and Slovakia a joint stock company is the only institutional form allowed. It is possible that a mutual association is regulated in some other laws. Lithuania is a special case allowing for an insurance undertakingsto be a public company, private company or Societas Europea.

Table 5: Legal forms of insurance undertakings

Country	Legal forms of insurance undertakings
Cyprus	joint stock company mutual association
Czech Republic	joint stock company co-operative
Estonia	public limited company
Latvia	stock company mutual co-operative insurance association
Lithuania	public company private company European company (Societas Europaea)
Hungary	joint stock company insurance cooperatives insurance associations
Malta	joint stock company mutual association
Poland	joint stock company mutual insurance society
Slovakia	joint stock company
Slovenia	joint stock company mutual association

Source: effective legislation of observed countries

Minimum amount of initial capital

Latvia, Lithuania and Poland denominate the minimum amount of share capital in euro, other accession countries in domestic currency. The latter are translated into the euro in Table 6 using the official exchange rates effective on 7 May 2004.

Under Estonian and Slovakian law, insurers must be incorporated as public limited companies.

The Czech Republic and Slovakia determine different amounts of minimum initial capital for different types of insurance. In Latvia, Hungary, Poland and Slovenia initial or share capital cannot be less than the minimum amount of guaranteed capital. Latvia, Hungary and Poland do not determine the minimum initial capital for reinsurance companies, while its level in The Czech Republic and Slovakia appears to be extremely high.

The exact amounts of initial or share capital differ significantly from country to country. Slovenia´s requirements are above average for the individual insurance types: for life insurance, Slovenia's required amount is among the three highest. Within non-life insurance Slovenia is the third-to fifth, for accident insurance its requirement is the highest, for property and credit insurance it is the third to fourth. For establishment of a re-insurance company Slovenia is the fourth highest in requirement among six countries with data on minimum required initial or share capital.

Guarantee fund

Except for Slovenia no other new EU Member State determines the minimum amount of guarantee fund for a re-insurance company. Estonia is the only one does not define guaranteed capital, but requires that

Table 6: Minimum amount of share capital (in million EURO)

Country	Life assurance	Non-life insurance				Reinsurance
		Liability insurance	Accident and sickness insurance	Property insurance	Credit insurance	
Cyprus	0,68	1,02				1,71
Czech Republic	2,79	2,79 4,84 6,21	1,86	1,86 2,79 6,21	4,84	31,04
Estonia	0,77	0,64	0,32	0,32	0,64	1,28
Latvia	3,00 (2,3*)	3,00 (2,3*)	2,00 (1,50*)	2,00 (1,5*)	3,00 (2,30*)	/
Lithuania	1,00	1,00	1,00			
Hungary	2,97	2,97	1,98	1,98	2,97	/
Malta	1,17	1,17				2,34 3,51°
Poland	3,00	3,00	2,00	2,00	3,00	/
Slovakia	1,99	3,74 4,98 1,49	1,25	1,25 3,74	3,74	24,90
Slovenia	3,02	3,02	2,01	2,01	3,02	3,02

Source: effective legislation of observed countries

* The amount in brackets is applied to the mutual association's minimum initial capital.

° This amount of minimum share capital must be paid, when the business of the insurance enterprise is not limited to reinsurance for risks located only in Malta.

Table 7: Minimum guarantee fund (in million EURO)

Country	Life assurance	Non-life insurance			
		Liability insurance	Accident and sickness insurance	Property insurance	Credit insurance
Cyprus	0,80	0,4	0,3	0,3 0,2	0,4 1,4
Czech Republic	2,79	2,79	1,86	1,86	2,79
Estonia	/	/	/	/	/
Latvia	3,00 (2,3*)	3,00 (2,3*)	2,00 (1,50*)	2,00 (1,5*)	3,00 (2,30*)
Lithuania	3,00	3,00	2,00	2,00	3,00
Hungary	2,97¤	2,97¤	1,98¤	1,98¤	2,97¤
Malta	0,93 (0,70*)	0,47¤	0,35¤	0,35¤ 0,23¤	0,47¤ 1,64¤°
Poland	3,00	3,00	2,00	2,00	3,00
Slovakia	1,00	1,00	0,75	0,75 0,50	1,00
Slovenia	3,02	3,02	2,01	2,01	3,02
EU standard	3,00	3,00	2,00	2,00	3,00

Source: effective legislation of observed countries

* The amount in brackets is applied to the mutual association's minimum guarantee fund.

¤ In the case of a mutual association, the minimum guarantee fund shall be reduced by 25 per cent.

° This amount is used, when the annual amount of premiums or contributions of the company due in respect of that class (credit insurance) for each of the preceding three financial years exceeded 2.92 million euro or 4 per cent of the total amount of premiums or contributions receivable by the company.

Remark: Cyprus, Lativa, Lithuania and Poland determine the minimum amount of guaranteed capital in Euro, other new EU members in domestic currencies, which were converted into € by the official exchange rates valid on May 7, 2004.

an insurance company's own funds (defined by the law) should be at least equal to the minimum share or initial capital of an insurance undertaking.

It is necessary to distinguish between the minimum initial capital and the minimum amount of guaranteed funds (defined generally as one third of the minimum capital, but not smaller than the guaranteed capital). As is well known, the minimum share or initial capital is defined as the starting investment into an insurance company regardless of the size of its business. The guaranteed capital on other hand, is defined by the size of its business, with criteria being the volume of premium, provisions, reserves, retained profit, etc.. Minimum capital is also determined by the size of business of the insurance company.

Where the numbers are equal in both tables 6 and 7, the laws determine that the minimum initial capital shoul be equal to the minimum amount of guaranteed capital. Table 6 shows quite significant differences between countries. Slovenia is slightly below average with its requirements. The Czech Republic and Slovakia again, have very high minimum capital requirements for reinsurance.

The EU determines the minimum amount of guaranteed capital, but not the minimum amount of initial capital. Information from the laws indicate that minimums are not harmonized among the new EU Member States, which may be a result of either not up-to-date information or permitted transition periods or the lack of its regulation within the acquis. Some countries are exactly at the EU directive levels with regard to minimum capital requirements (Poland, Lithuania, Latvia), The Czech Republic is close, but others differ substaintially from them.

Slovenia is among the first four out of 9 accession countries with the highest level of required guaranteed capital for all types of non-life and life insurance.

Insurance technical provisions

The EU directives regulate only some of the technical provisions, known to the new laws of the new EU Member States. Directives regulate the manner of the methods of calculation of tehnical provisions (mathematical and damage provisions in more detail), but the field of technical provisions generally speaking is not completely harmonized.

Table 8 indicates that Polish law recognizes the greatest number of types of provisions, followed by the Czech, Slovak and Slovene law. On other hand, the law in Malta regulates only two types of technical provisions. The Latvian solution is special in that it enumerates some additional specific provisions, not known to any other new EU Member States.

For all new EU Member States it is typical that it is not defined in detail how to form and calculate provisions.

Table 8: Insurance technical provisions

Country	Provisions for unearned premiums	Provisions for claims	Equalization provisions	Mathematical provisions	Provisions for bonuses and rebates	Provision for insurance where the investment risk is borne by the policyholder	Provisions for unexpired risks	Other technical provisions
Cyprus	✓	✓	✓	✓			✓	✓
Czech Republic	✓	✓	✓	✓	✓	✓		✓
Estoniaa	✓	✓	✓	✓	✓			✓
Latvia	✓		✓	✓				✓
Lithuania	✓	✓	✓	✓	✓			✓
Hungary	✓	✓	✓	✓				✓
Malta		✓	✓					
Poland	✓	✓	✓	✓	✓	✓	✓	✓
Slovakia	✓	✓	✓	✓	✓	✓		✓
Slovenia	✓	✓	✓	✓	✓	✓		✓
EU directives	✓	✓	✓	✓			✓	

Source: valid laws of analysed countries

Bodies of insurance undertakings

The issue is institutionalization (organization) of the basic principal-agent problem related to corporate govenrnance.

The laws of the new EU member states do not determine explicitly which bodies an insurance company should have. But implicitly, that information can be obtained from provisions in the laws.

Table 9: Bodies of an insurance undertakings

Country	Bodies of an insurance undertaking		
	AGM	Management board	Supervisory board
Cyprus	✓	✓	
Czech Republic	✓	✓	✓
Estonia	✓	✓	✓
Latvia	✓	✓	
Lithuania	✓	✓	✓
Hungary	✓	✓	✓
Malta	✓	✓	
Poland	✓	✓	✓
Slovakia	✓	✓	✓
Slovenia	✓	✓	✓

Source: effective laws of AC-10

Annual General Meeting (of shareholders) and Management board are mentioned in the laws of all new EU member countries. Cyprus, Lativa and Malta do not mention the Supervisory Board in their laws. This can be a consequence of the fact that they have one-tier organization of stock companies, or just a consequence of a lack of reference to this body in the law. Slovenia is not different from other new EU member countries by having all three usual bodies.

All new EU member countries determine in their laws that insurance companies should have their own actuary and internal audit. The only exception is Poland which does not regulate internal audit in existing insurance law.

Required qualifications for a board member of an insurance company

For successful corporate governance of insurance the quality of the management board is an important determinant. None among the AC-10 group regulates the term of office for board members of an insurance company. Only Poland (3), Slovenia (2), and indirectly Hungary (2), determine the minimum number of Board members.

Only Poland and Slovenia require that some Board members should speak the local language, 2 in Poland, at least 1 in Slovenia. The Czech Republic, Poland and Slovenia do not allow for members of the Board to be simultaneously a member of a Board in another insurance, trade, company or bank. This is not interdicted if the member of the Board of a parent company wants to also become a member of the Board of a subsidiary company.

EU sets the threshold for minimum capital requirement, but not for initial capital.

PARTICULARITIES OF THE REGULATORY FRAMEWORK IN SLOVENIA

Comparison of regulatory framework in the new EU member countries confirms the statement of the EC EU from June 2003 holds, namely that Slovenia among all the EU accession countries has the best prepared insurance sector, comparable only with Malta and Cyprus with their long time tradition of a market economy. Some of the requirements from the acquis are fullfilled in Slovenia unconditionally, others with some alterations or particularities.

a) The fields of full compliance with the acquis in Slovene insurance regulation are:

– equal qualifying holding of shares as generally requested (10%, 20%, 33%, 50%);

– permits both basic statutary forms of organizations of insurance companies, stock holding company and mutual association;

– has three classical bodies in a two-tier system of corporate governance: AGM, management board and supervisory board.

b) On other hand, particularities in regulatory framework of Slovene insurance companies are:

– discretionary period for the supervisory agency to decide upon an application for authorisation to establish a new insurance company;

– insurance is supervised by a special agency, which is not merged with the supervisory bodies for banks and capital markets (similar to the half of the new EU member countries),

– does not allow the establishment of new composite insurance companies, but allows composite insurance companies already in existence at the time of enaction of the new insurance law to remain intact,

– Slovenia has higher than average requirements regarding minimum initial capital, which are practically equal to the minimum guarantee capital requirements (again, above average),

– has three types of technical provisions – more than what is required by the EU insurance directives, but does not have the required provisions for unexpired risk,

– among required qualifications for a management board member of an insurancy company, university education is not listed explicitly in Slovene law, but requirements for experience are above average (4 years in managing an insurance company), the reputation requirement is not included, while the non-sentencing request is only mild.

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Table 10: Eligibility criteria for a member of the Management board of an insurance undertaking

Country	Education	Experience	Reputation	Other
Cyprus	special knowledge	experience in financial field	good repute	was not convicted for some criminal offences; Cyprus resident
Czech Republic	/	professional experience	good repute	has not been finally sentenced for some criminal acts
Estonia	academic education	experience of working in the field of insurance or other financial services	impeccable reputation	has not caused the bankruptcy of a company
Latvia	necessary education	not less than 3 years work experience in the relevant field	unim-peachable reputation	Latvian resident; has not been deprived the right to perform commercial activities; has not been convicted of an intentional criminal offence
Lithuania	professionally qualified	professionally experienced	good repute	has not been convicted for any premeditated criminal acts; does not abuse drugs or alcohol
Hungary	university degree	at least 5 years of experience in the field of insurance or similar	good business reputation	no prior criminal record
Malta	university degree	1, 2 or 4 years of experience depending on work (job)	integrity	has not been convicted of a criminal act
Poland	higher education	experiences that provides warranty to conduct the insurance undertaking matters in due fashion	/	was not convicted of a willful crime; possesses full capacity to undertake legal transactions
Slovakia	university degree	at least 3 years practice in the field of financial markets	/	/
Slovenia	satisfactory theoretical and practical knowledge	at least 4 years of experience in insurance or other similar company	/	has not been finally sentenced for more than three months of imprisonment

Source: effective legislation of new Member States

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8. Polish Law: Act on Insurance Activity (22. 5. 2003)

9. Slovakia's Law: Act on Insurance Industry No. 95 (1.2.2002)

10. Slovenian Law: Insurance Act (27. 1. 2000; Ur.l. 13/2000), Act on Modifications and Amendments to the Insurance Act (1. 3. 2002, Ur.l. 21/2002), Act on Modifications and Amendments to the Insurance Act (21. 4. 2004, Ur.l. 50/04)

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Bancassurance and NLB Group: A Case of NLB Vita

*Marjan Kramar and Miran Vičič**

BANCASSURANCE AND NLB GROUP: A CASE OF NLB VITA

After the description of some possible bancassurance models, we conclude that the ultimate model does not exist. Taking into account the local environment and the corporate culture of the business partners involved, the most appropriate model has to be decided and defined case by case.
Why bancassurance? After considering the perspective of both client and the financial organization, we conclude that bancassurance starts as mainly a distribution issue, quite often by offering insurance products through bank outlets, but is expanding to use the strengths of an integrated financial services group combining the know how of the insurer, the asset manager and bank departments.
Entering the Silver Century, we believe in the high market potential of life insurance business. By offering the client tailor-made modern life insurances, we are making the global NLB product-offer broader and more diversified. With NLB Vita, by creating a new life insurance company acting mainly as a product factory offering its tailor-made products through the NLB network, we are convinced we have chosen the right model.

Bancassurance is a complex activity well known in the developed capital markets. In Slovenia it began to emerge with NLB's introduction. Its basic definition, or at least its minimal criterion, is actually marketing banking and insurance products and their combinations through banks and their distribution channels. The definition is often even restricted to an offer of insurance products via trained sales staff in bank branches, whether a complete sales process is carried out in the branch, or the client is directed to the the sales staff of the insurance services (e.g. agents).

From an agent to a bank insurance company[1]

It is not possible to provide a uniform definition, as it is not possible to prescribe the ultimate model of bancassurance. Every business decision on introducing bancassurance has to be taken on case by case basis whereby the specific environment and corporate culture of both partners need to be observed. Banks with a wide range of retail products and services have some advantage against the insurance companies. The main advantage is their knowledge of and access to a huge customer base, a well established branch network in a broader area, and their image in the environment where they operate. The latter is inevitably linked to a high degree of trust.

Well known bancassurance models are based on how strong the connection between the bank and the insurance company is. Every sales model has its strengths and weaknesses. The bank

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[1] From materials: Bancassurance deals and models; Insurance Advisory Board, August 2002.

may either be an intermediary, set up a joint enterprise with the insurance company, carry out a merger between the two entities or an acquisition of the insurance company, or set up a special insurance company as a functionally integrated part of the bank. Each model has its strengths and weaknesses.

Interchange of advantages for the customer and the bank

Bancassurance usually emerges as an idea of exploiting joint distribution channels. However, it has to be upgraded and must fully exploit the power of an integrated bank group in order to maximise the value of related or ancillary activities. Using bank officers in branches to sell other services creates additional (non-interest) income and thus lowers high fixed costs of the bank network. Nevertheless, creating added value is not restricted to sales activities but it can be upgraded by offering complex services adapted to a customer which fully exploit the know-how of the insurance company, the bank and the asset manager.

A case of exploiting the bancassurance potential was successfully defined by *Boston Consulting Group*. Banks offering new products to their existing clients can double their income with the insurance and investment products. Advantages affected by such sales models can be observed from the customer's as well as the financial organisation's view.

Every customer is interested in the bancassurance approach of his/her bank. The customer expects his/her banker to provide good advice and to present all options and products related to asset management (bank loans and deposits, securities and insurance products). The banker is successful if the customer is able to purchase all services related to managing his / her financial matters in one place (a so-called one-stop-shop).

Insurance against personal risk (life insurance, disability insurance and critical illness insurance products) must be considered as added value to a range of financial products and activities, all within the expectations and envisions of the customer. Similar aspects apply to risk coverage connected with traditional bank products such as insurance in the event of death when taking out a loan.

The fact is that wealthier customers are becoming increasingly demanding. Therefore financial institutions are forced to offer a wide range of simple as well as sophisticated financial products, including insurance.

Bancassurance enables financial organisations to offer their clients an up-to-date and wide range of products which cover the customers' needs throughout their lifespan and offer them appropriate asset management. This is a way to gain greater loyalty and attachment of the customers. Bancassurance allows the customer to satisfy a greater scope of needs whereby it enables the customer to satisfy several of his/her needs from one supplier which is important, not only for creating new sources of income, but also for retaining the existing one. The target of every business subject is to acquire as big a scope of their clients operations as possible before the competition makes an offer of an equal or similar business.

Wrapping up banking and insurance products in bankassurance creates new opportunities.

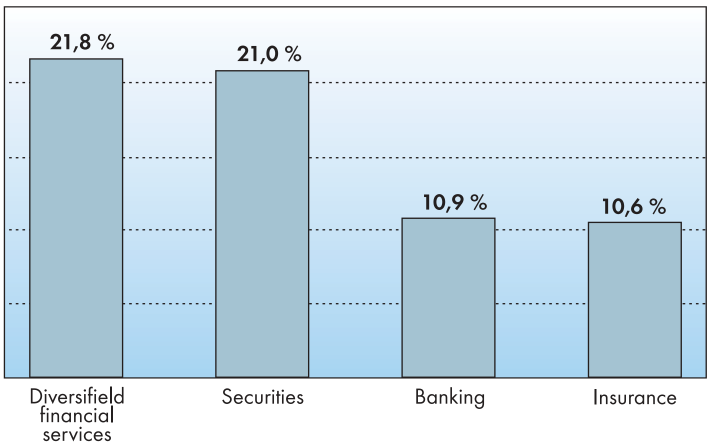
Return on Equity (ROE) in financial institutions which offer a wide range of financial services is usually higher than in those which offer either only banking or only insurance services (Graph 1, *Swiss Re* research, 2001).

The strongest advantage of banks are their customer base, a desire for cross selling and their efficient and integrated business processes. Connecting and integrating banking and insurance services creates numerous opportunities. A customer who has taken out a loan is offered life insurance in order to protect his/her family. If the customer also wishes to invest in the capital markets, we offer him/her insurance linked to the units of funds, so, in connection with the insurance product, we take advantage of the asset manager's expertise as well.

Developed markets and bancassurance

Bancassurance has attained the greates success in the life insurance area. Property insurance offers over the counter are at much lower level despite some visible progress, particularly in France.

Graph 1: Return on Equity (ROE) in financial institutions (a breakdown in respect of a prevailing kind of offer)



Source: Swiss Re, No.7/2001

In the markets like France, Spain and Italy, more than 50 percent of life and pension insurance premiums are collected over the counter. The data is amazing, given that two decades ago banks were practically not present in bancassurance.

Belgium market development of individual life insurance between 1994 – 2000 (Graph 2) shows an increased share of sales in banks from 28 to 68 per cent, while concurrently the sales via traditional insurance channels (agents) fell from 60 to 31 per cent. However, the sales volume via traditional channels did not decrease, only the total collected premium sharply increased, mostly on account of over the counter sales.

In Germany, Great Britain and the USA the traditional way of selling insurance services still prevails although bancassurance is increasingly recognized. There are different reasons for that. In the past bancassurance was often subject to statutory restrictions. Some reasons can be found in *the Overview of the European Bancassurance Market; Insurance Advisory Board, November 2003*.

According to NLB, one of the key elements of success are products which already developed in line with the general bank's offer, adapted to in bank branches and a possibility to sell via adequately trained and licensed bank officers.

In the Anglosaxon markets bancassurance has not expanded as much as in France. There bankassurance models prevail whereby bank branches direct their customers to insurance agents, or the bank officers direct the agents to customers, potential buyers of an insurance product. Joint performance of the insurer and the banker is of key significance, albeit difficult to achieve. Such banking and insurance structures are usually less integrated and less cost-effective.

Table 1: Life insurance sales in respect of marketing channel in % (in 2002 and projection in 2007)

	Banks&bancassurance		Connected agents		Direct sales		Intermediaries		Other	
	2002	2007	2002	2007	2002	2007	2002	2007	2002	2007
Spain	77	81	–	–	3	1	20	18	–	–
France	61	67	8	5	6	6	9	9	16	13
Italy	56	66	34	30	9	3	1	1	–	–
Germany	19	24	51	54	9	6	21	16	–	–
United Kingdom	18	28	17	13	–	–	56	52	9	7

(France:other = company employees; Germany:direct sales value includes other; VB: connected agents value includes direct sales; other= telesales, etc.)
Source: Datamonitor

Marketing life and non-life insurance

The reasons why banks which offer bancassurance with life and pension insurances hold big market shares are in that there is a close link and a similarity between them and the traditional banking products that enable an overall offer to manage the client's assets. Apart from savings and investment products, the life insurance offer gives the banks a substantial competitive advantage over other providers of financial services and makes them the only ones to have an overall offer of all products.

The changing demographic situation in developed countries, as well as in Slovenia, significantly encourages and provides advantages to develop long-term savings products which provide protection in old age. Tax relief in many countries directly particularly encourages additional pension insurance and other similar products.

The range of products spreads from the long-term products based on the capital / principal accumulation, and family protection whereby savings are converted into an annuity in perpetuity. We should not ignore the fact that life insurance products can be used as a legal option of transferring property to younger generations (inheritance) tax-exempt.

Some property insurance products also have many features similar to the banking products or they can be linked with them: homeowner's insurance could be combined with housing loan sales, motor vehicle insurance with selling loans for motor vehicle purchase. We should, however, be aware of some risks the bank is exposed to. Arranging insurance claims, in particular any related court disputes can affect the general perception a customer has of the bank. Training bank officers to handle these products is essential and more demanding because these products are not very similar to banking ones, e.g. life insurance product. And finally, property insurance markets are usually substantially more developed and stable so that acquiring a significant market share can be connected with a risk of acquiring 'unsuitable' customers.

Why a life insurance company?

There are several reasons why NLB decided to set up a life insurance company, or to develop an offer of life insurances. In the Slovenian insurance market the property insurance offer still prevails even though the larger share of premium income derives from life insurance policies (annually 10 – 20 per cent). However, as opposed to the volume of banking operations and the life insurance premium income in Western Europe, the total income on account of life insurance policies is still relatively low, thus in 2002 amounting to 60.56 billion tollars and in 2003 to 71.33 billions tolars. We estimate that the life insurance market potential in Slovenia is much higher than in the area of non-life (property) insurance. Given that the offer of life insurance products resembles much more the traditional banking operations than the property insurance, it made sense to focus first on life insurance. Yet this decision does not exclude a possible offer of property insurance in the future (a new insurance company next to NLB Vita since under law NlB Vita may not take up the non-life business.

When selecting a business model, we have avoided merger or a takeover of an insurance company for many reasons and have decided to establish a new insurance company.

If we wish to sum-up the Slovenian life insurance market in only one word, we can use the word "traditional" despite constant changes in this field. As for insurance distribution, the market of insurance representatives and intermediarys (agents) prevail, but there are various financial institutions which recently initiated bancassurance activities (Zavarovalnica Maribor and NKBM, Abanka and Zavarovalnica Triglav). As to life insurance offer, most premium income is generated on account of classical mixed life insurance (with advance payment of the representative or intermediary commission). Investment life insurance emerged in Slovenia in 2002; most of the premium on account of these insurances is accumulated by the capital fund in compliance with the pension legislation, and not only via individual life insurances.

Furthermore, we wished to avoid the problems of culture differences opposing each other when taking over or acquiring a company. We also did not want to sell similar products via completely different marketing channels. And finally, as it is true in other countries, public opinion on the banks' reputation is much higher than the one on the insurance companies' reputation.

Advantages of NLB and KBC: NLB Vita

As to the establishment of a new life insurance company which will offer customers adjusted, flexible and transparent products, mostly via the NLB branch network, we decided in favour of a Greenfield approach as the most suitable and success generating one, provided both parties are involved. NLB Vita, življenjska zavarovalnica, d. d., Ljubljana acquired a licence and was registered on 4 June 2003. It was set up by NLB and its strategic partner KBC Insurance, each contributing half of the capital input. The main reason for its establishment was to combine NLB's competitive advantage as the strongest bank in Slovenia (with the strongest brand name, a vast customer database and a high trust rate) with KBC's know-how and experience in the area of insurance, investment banking and management, as well as IT.

NLB Vita is above all a productive plant. This means that NLB Vita focuses on developing products which will enable NLB to offer modern life insurances adjusted to customer needs any moment and are suitable for over the counter sale. Cooperation with marketing and the NLB distribution network is essential either in planning the development of new life insurances or in setting targets, sales plans and other activities. A very significant key element in marketing is the IT support or application software developed by NLB which facilitates and helps bank officers to provide modern and professional advice to a customer.

NLB Vita is cost-effective with a limited, albeit well qualified number of workers in the support office (NLB Vita actually employs 12 people full time), dealing with administration (conducting the policies) and solving damages. It abides by all statutory provisions and requirements applicable to companies (accounting, reporting...) like any other insurance company. NLB Vita represents an increasingly important source of income for NLB coming from insurance commissions and dividends.

Traditional distribution channels still preferred by German, British and USA insurers.

For NLB it is highly significant that it can offer its clients new up-to-date life insurance services whereby it rounds off, supplements and enlarges its overall offer. NLB Vita is thus integrated in the NLB complete packet of investment and savings products (from traditional deposits and mutual funds to life insurance) to satisfy the ever new needs of more or less discerning customers.

In the initial phase we focused particularly on wealthier customers. From its vast database NLB can offer its customer life insurance which also means a high cross-selling potential. By offering life insurance (and other non-traditional banking products) NLB can offer a broader range of financial services an individual customer would enquire about (»share of wallet«). Such a vast and up-to-date offer can also attract customers of other bank and insurance companies. Over a period of time, we will develop products designed for the SME owners.

In compliance with the statutory requirements related to the insurance representation and mediation in Slovenia, life insurance is offered via the NLB branches (soon via the NLB Group operating network). This means that we follow the exclusive sales concept: NLB Vita will not establish a separate agency network to sell insurance within the existing concept. Initially we invested substantially in training of intermediarys (not only big investments related to acquiring the intermediary's licence via the Slovenian Insurance Association, but also investments in internal training) which we regularly update.

KBC – Belgian strategic partner

The project well suits the KBC development strategy of the second domestic market in Central Europe. The development of bancassurance as well as insurance and financial activities (albeit the latter is not included in the NLB Vita approach) is the KBC Group's strategic base. KBC's standard model is a multi-distribution approach. NLB estimates that, taking in consideration special aspects of the Slovenian market, the NLB Vita model is a conscious selection of all parties involved. The following figures will demonstrate the KBC's position: in 2003 the KBC's life insurance premium income amounted to over 2,400 mio euro (1,689 mio euro in 2001 and 2,246 mio euro in 2002). KBC AM, the subsidiary company, manages assets of 89,000 mio euro.

Financial services on one spot

Up-to-date savings and investment family protection life insurances (life insurance in the event of death, fatal disease and accidental death) are a response to changing and ever new customer needs for savings and investment products; falling deposit interest rates compel customers to look for new investment opportunities. As a result, long-term products of the second and the third pillar (which complement statutory pension and retirement schemes) are definitely increasingly important.

Our aim is to advise on life insurances and include them in a comprehensive offer satisfying even the most specific customer needs. Adaptability, transparency (e.g. cost transparency) and family protection on top of that are important advantages of our life insurances.

Our objective is to offer Slovenian customers up-to-date and quality life insurances. Whoever wants to be more successful and take advantage of being the first on the market must be capable of launching a new product in the shortest time possible. A new NLB Vita product usually takes four to eight weeks to create, depending on the product. Last year we launched ten new life insurances in six and a half months.

Bold NLB Vita aims and NLB bancassurance activities

Our professional advice and high quality innovative products aim at adapting to and meeting the growing and changing customer needs for accumulating, managing and protecting their savings. We want to achieve a large and stable market share.

The objective is to establish the ultimate bancassurance activity in Slovenia and achieve at least an 8 per cent share in the life insurance market in five years.

In 2003 a six-month market operating activity brought us a 3.2 per cent market share (2.4 million tolars in premium income). Focusing on purely individual life insurances alone which NLB Vita is actually working on (excluding pension and health insurance), the market share is 4 per cent. In the field of individual investment life insurances we gained a market share that even exceeds 39 per cent which is an indicator that this business is relatively young in Slovenia.

NLB Vita will be in the black in 2005. Short-term achievement of targeted goals will not be easy, given that life insurance is a long-term product (more than 10 years due to sales tax of insurance transactions) and the fact that the customers are not as keen on traditional life insurances which are not long-term orientated. Furthermore, life insurances are not subject to tax relief. On the contrary, insurance sales tax of insurance deals of 6.5 per cent is even one of the highest in Europe; individual life insurances in most EU countries are tax exempt.

It is however essential that the base of targeted goals is set realistically:

1. In general, the life insurance market potential is very high, much to the changing demographic situation. We're entering 'the Silver Century[2] , or a growing share of the elderly in total population, a prevalent world trend. Additionally, increased life expectancy enables the elderly to spend more time in retirement.

Product diversification is crucial especially if we consider (also the international) the environment with traditional banking products, offering increasingly lower interest rates.

2. We believe we have selected the right product because NLB Vita, as a newly established company connected with NLB and KBC offers and exploits the significant advantages of the scope and quality which both founders already have (costs, proceedings, know-how...) And finally, we believe in added value with the products the NLB network can capitalise on and it can offer its clients a comprehensive financial service.

Conclusion

Financial institutions as well as their clients have a clear interest in bancassurance development, now increasingly changing from a purely distribution concept to an offer concept of integrated financial services with the aim to maximize the values within the financial group.

It is not a question whether to opt for bancassurance or not but how to tackle it. Only those market players will be successful in the market who will successfully adapt the model to content, market conditions and needs.

The key factors for creating a model are as follows: clear joint business objectives, quality and innovative ideas when offering services (the first offer advantage), short period of development and preparation of a service, cost-effectiveness, well trained and motivated sales staff in branches who provide professional advice to customers. All this with a view to creating a strong and long-term relationship with the client and satisfy as many of their needs for financial products as possible.

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Empirical Analysis of the Insurance Sector in New EU Members States

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EMPIRICAL ANALYSIS OF THE INSURANCE SECTOR IN NEW EU MEMBERS

The paper presents a detailed picture of the insurance market in the 10 new EU Member States before their accession to the EU (in 2002). General financial and specific insurance indicators are discused first (in comparison with the existing EU-15 countires), correlation analysis among major indicators is then reported and the regression analysis helps to reveal the rules of behavior in these countries. They are far less developed in insurance than the old EU Member States. Special reflection among all EU-10 is given to Slovenia. It is among the most developed accession countries with a relatively high insurance awareness (especially in non-life insurance). It does not differ significantly in insurance behavior from the other nine new EU Member States.

In May 2004, Slovenia became a new member state of the enlarged EU-25 together with nine other countries. Similarly to other fields, new legislation was adopted in insurance and competitiveness increased in the domestic market. What are the conditions in this market? How competitive is the Slovene insurance sector in comparison to insurance in the other new EU Member States and in comparison with old EU members?

In this article the situation in the insurance sector of the 10 new EU member states is analyzed with regard to the average of the old EU-15 countries and with special regard to the relation of the Slovene insurance sector to both, the old and the new EU Member States.

Accession to the EU should bring certain substantive changes in the insurance sector of new EU Member States, according to analysts of the Swiss-Re (2002). Growth in insurance premiums, especially life, should be faster than in the old EU-15, privatization will continue with increased entry of foreigners and fulfillment of new EU insurance directives will cause problems in some new EU member states.

The actual situation is described by a large volume of data for each of the 10 new EU Member States (EU-10) and for the average of the EU-15 in 2002 (the last available complete set of data) and partly for the period 1992-2002. They are presented, first, in the form of basic absolute series and later in the form of general financial coefficients and special insurance coefficients. Next, regularities in behavior of the insurance sector in the EU-10 are

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Table 1: Basic series of Insurance in the new EU-10 and averages for the EU-15, 2002

CY	CZ	EE	HU	LT	LV	MT	PL	SI	SK	AC10	EU15	
GDP, mio €	9582	72244	6889	72047	13901	8516	4500	220307	24579	25788	458353	9160000
POP, mio	0.715	10.201	1.356	10.155	3.46	2.332	0.385	38.609	1.996	5.378	74.587	376
ER	1.742	0.032	0.064	0.0042	0.2899	1.6393	2.3887	0.295	0.0047	0.024		1.0
PREM, mio €, 92	167	590	.	586	.	.	55	1100	219	172	2889	359575
PREM, mio €, 97	320	1256	67	863	85	103	115	3141	700	442	7092	537736
PREM, mio €, 02	486	2885	139	2097	215	169	185	6790	1242	872	15080	820367
PREML	260	1085	29	859	40	7	85	2883	282	377	5907	
PREMNL	226	1799	110	1238	174	162	100	3907	960	495	9171	
BDPPOP	13401.40	7082.05	5080.38	7094.73	4017.63	3651.80	11688.31	5706.10	12314.1	4795.09	6145.21	24361
PREM/BDP	0.051	0.040	0.020	0.029	0.015	0.020	0.041	0.031	0.051	0.034	0.033	0.0895
PREMPOP	679.720	282.815	102.507	206.499	62.139	72.470	480.519	175.866	622.244	162.142	202.180	2181
PREMLBDP	0.027	0.015	0.004	0.012	0.003	0.001	0.019	0.013	0.011	0.015	0.013	
PREMNLBDP	0.024	0.025	0.016	0.017	0.013	0.019	0.022	0.018	0.039	0.019	0.020	
PREMLPOP	363.636	106.362	21.386	84.589	11.561	3.002	220.779	74.672	141.283	70.100	79.196	
PREMNLPOP	316.084	176.355	81.121	121.910	50.289	69.468	259.740	101.194	480.962	92.042	122.957	
PREMLPREM	0.535	0.376	0.209	0.410	0.186	0.041	0.459	0.425	0.227	0.432	39.200	62.700
harmonization	9.000	9.000	8.000	8.000	7.000	9.000	9.000	9.000	9.000	8.000		
avge rgdp 9202	2.200	3.000	5.600	0.400	4.400	6.000	2.000	3.700	6.000	2.500	2.200	2.100
avge rprem 9202	7.200	7.500	12.100	6.700	17.400	11.600	8.700	9.300	10.800	8.700	8.900	5.700
avge rpreml 9202	8.600	11.900	28.600	14.300	7.600	–15.200	16.700	14.800	23.900	13.800	13.900	8.200
avge rpremnl9202	5.800	5.600	9.800	3.600	21.100	15.100	4.900	6.600	8.900	6.000	6.700	2.600
avge rinv 9202	10.100	2.900	19.600	12.800	.	18.300	5.500	32.100	6.300	–0.700	10.800	7.700
avge rprempop22	5.600	7.600	13.500	6.900	18.900	9.500	8.300	9.200	10.800	8.400	7.800	5.400
invl/inv	86.700	72.400	41.200	45.700	8.200	31.200	64.500	61.900	38.500	79.900	61.700	81.100
no companies 92	42.000	12.000	19.000	13.000	24.000	15.000	22.000	27.000	7.000	9.000	190.000	4974.000
no companies02	34.000	42.000	13.000	26.000	38.000	20.000	18.000	72.000	14.000	27.000	304.000	4538.000
kr nocomp 0292	0.810	3.500	0.684	2.000	1.583	1.333	0.818	2.667	2.000	3.000	1.600	0.912
no compF 92	17.000	9.000	19.000	6.000	24.000	15.000	5.000	20.000	6.000	7.000	128.000	
nocompF 02	21.000	35.000	6.000	3.000	38.000	14.000	5.000	23.000	11.000	8.000	164.000	
% compF 92	0.405	0.750	1.000	0.462	1.000	1.000	0.227	0.741	0.857	0.778	0.674	
% compF02	0.618	0.833	0.462	0.115	1.000	0.700	0.278	0.319	0.786	0.296	0.539	
%AC10 prem 92	22.100	6.300	10.000	6.800	12.600	7.900	11.600	14.200	3.700	4.700	3.700	96.300
%AC10 prem02	11.100	13.800	4.300	8.600	12.500	6.600	5.900	23.700	4.600	8.900	6.300	93.700
%AC10 preml 02	4.400	18.400	0.500	14.500	0.700	0.100	1.400	48.800	4.800	6.400	1.100	98.900
%AC10 premnl02	2.500	19.200	1.200	13.600	1.900	1.800	1.100	42.800	10.500	5.400	2.900	97.100
K5 nl 97	46.100	86.700	61.700	89.000	.	63.600	62.000	85.200	93.700	90.400	82.300	
K5 nl 02	45.500	82.700	91.600	86.700	.	75.600	73.000	82.100	94.300	87.300	83.400	
K5 l 97	91.700	93.800	96.400	88.900	.	94.600	100.000	98.500	89.100	91.100	92.700	
K5 l 02	88.500	79.400	99.100	80.600	.	99.000	100.000	88.700	87.400	76.600	85.200	
no empl 92, 000	1.000	9.317	1.000	14.100	0.950	0.900	0.719	20.500	3.000	3.525	55.011	909.522
no empl 02, 000	1.660	15.740	1.493	28.000	1.500	1.786	0.933	30.617	5.204	7.622	94.555	870.468
prem/empl 02	292.771	183.291	93.101	74.893	143.333	94.625	198.285	221.772	238.663	114.406	159.484	942.
empl/pop 02	2.322	1.543	1.101	2.757	0.434	0.766	2.423	0.793	2.607	1.417	1.268	2.425
%AC10empl 02	1.800	16.600	1.600	29.600	1.600	1.900	1.000	32.400	5.400	8.100	9.800	
inv 92, mio€	349	2004	.	608	.	.	222	361	467	575	4587	1686055
inv 02, mio €	1330	6311	158	3797	308	152	553	14843	1738	1182	30374	4720835
kr inv 0292	3.811	3.149		6.245			2.491	41.116	3.722	2.056	6.622	2.800
%AC10 inv 02	4.400	20.800		12.500	1.000	0.500	1.800	48.900	5.700	3.900	0.600	99.400
invl 02, mio €	1152.000	4572.000	65.000	1736.000	25.000	48.000	357.000	9183.000	669.000	944.000		
invnl 02, mio €	177.000	1739.000	93.000	2061.000	283.000	105.000	197.000	5661.000	1070.00	238.000		
benefits/preml 01	16.900	81.400	56.500	57.700	.	52.500	15.500	37.300	287.900	39.000	57.100	100.100
admexpL 01,mio€	30.000	98.000	3.000	79.000	.	2.000	.	532.000	39.000	104.000	887.000	
prnl motor 02 mio	99.000	931.000	71.000	696.000	106.000	77.000	49.000	2536.000	355.000	288.000	5209.000	
prnl mot 01 comb	100.900	.	.	.	.	93.900	108.600	103.400	103.800	.	103.1 cea	
prnl health 02 mio	40.000	56.000	5.000	48.000	11.000	26.000	19.000	222.000	391.000	13.000	832.000	
prnl hea 01 comb	68.600	.	.	.	.	92.900	82.000	78.400	97.200	.	101.400	
prnl proper 02 mio	44.000	408.000	25.000	404.000	28.000	28.000	21.000	717.000	137.000	135.000	1947.000	
prnl liabil 02 mio	10.000	231.000	3.000	52.000	7.000	15.000	5.000	133.000	27.000	30.000	513.000	
% prem mot/nl	0.438	0.518	0.645	0.562	0.609	0.475	0.490	0.649	0.370	0.582	0.568	
% prem hea/nl	0.177	0.031	0.045	0.039	0.063	0.160	0.190	0.057	0.407	0.026	0.091	
% prem prop/nl	0.195	0.227	0.227	0.326	0.161	0.173	0.210	0.184	0.143	0.273	0.212	
% prem liab/nl	0.044	0.128	0.027	0.042	0.040	0.093	0.050	0.034	0.028	0.061	0.056	
% prem prop/gdp	0.005	0.006	0.004	0.006	0.002	0.003	0.005	0.003	0.006	0.005	0.004	
% prem hea/pop	55.944	5.490	3.687	4.727	3.179	11.149	49.351	5.750	195.89	2.417	11.155	
% prem mot/gdp	0.0103	0.0128	0.0103	0.009	0.0076	0.0090	0.0108	0.0115	0.0144	0.0111	0.0113	
invest/prem	2.7366	2.1875	1.1366	1.8106	1.4325	0.8994	2.9891	2.1860	1.3993	1.3555	2.0141	5.754
invest/BDP	0.1388	0.0873	0.0229	0.0527	0.0221	0.0178	0.1228	0.0673	0.0707	0.0458	0.0662	0.515
prem/comp	14.29	68.69	10.69	80.65	5.657	8.45	10.27	94.30	88.71	32.29	49.60	180.78
empl/comp	0.048	0.374	0.114	1.076	0.039	0.083	0.051	0.425	0.371	0.282	0.311	0.192
krcompf	1.526	1.111	0.462	0.249	1.000	0.700	1.225	0.430	0.917	0.38	0.800	
DRŽAVE	CY	CZ	EE	HU	LT	LV	MT	PL	SI	SK	AC-10	EU-15

Source: CEA, eco: European Union Enlargement 2004, Paris, Brussels, 10/2003

LEGEND:

admexpl	= % of administrative expenses in life insurance premiums, 2001
avgergdp	= average yearly growth rate of GDP in 1992–2002, %
avgerinv	= average yearly growth rate of insurance investments, 1992-2002, %
avgerprem	= average yearly growth rate of premiums, 1992–2002, %
avgerprpop	= average yearly growth rate of premiums per capita, 1992-2002, %
bdp02	= GDP in 2002, in € billion,
gdppop	= GDP per capita, 2002; in €
benefits/preml 01	= paid-out benefits over paid-in premiums in life insurance, 2002
compf	= share of insurance companies in domestic ownership, 2002,
emplcomp	= employees per insurance company, 2002
emplopop	= share of employment in insurance sector in total employment, 2002
harmon	= harmonisation with Acquisom, dummy variable
inv	= investment of insurance sector, in € million
invgdp	= share of investment of insurance sector in GDP
invl/inv	= share of life insurance investment in total insurance investment, 2002
invprem	= ratio of insurance investment in premiums, 2002
K5l	= concentration coefficient: share of the 5 largest life insurance companies in premiums
K5nl	= concentration coefficient: share of the 5 largest non-life insurance companies in premiums
krcompf	= growth coefficient of the share of domestic insurance in total insurance companies, 2002/1992,
no	= number (insurance companies, employees, etc.)
pop02	= population in 2002,
prem	= premiums, in Million €,
premgdp	= premiums/GDP, 2002, %; penetration coefficient
premcomp	= premiums per insurance company, 2002, in Million €
premempl	= premiums per insurance employee, in Thousand €
prempop	= premiums per capita, 2002, in €; density coefficient prnl mot (health, property liability) = premiums for all kinds of non-life insurance, Million €
% AC10	= % of one EU-10 member state in total for all EU-10
% prem mot (health, property)/nl	= % of one type in total non-life premiums, 2002
CY	= Cyprus
CZ	= Czech Republic
EE	= Estonia
HU	= Hungary
LT	= Latvia
LV	= Lithuania
MT	= Malta
PL	= Poland
SI	= Slovenia
SK	= Slovakia
AC10	= 10 new EU Member States
EU15	= 15 old EU Member States

analyzed, first with correlation analysis and later with regression analysis. The final goal of this analysis is to find out how prepared the Slovene insurance sector is to enter the insurance market of the enlarged EU-25 and what will be its opportunities to develop further at home and abroad. The study should give an answer to the following particular questions:

– how much does the insurance sector of the new EU-10 lag behind the insurance sector in the old EU-15 ?

– what are the particularities of the insurance sector in the EU-10 ?

– what is the position of the Slovene insurance sector among them all ?

The analysis indicates that the insurance sector of new EU-10 lags substantially behind the insurance sector in the old EU-15. At the same time, insurance in Slovenia is more developed than in all other transition countries.

THE SITUATION IN THE INSURANCE SECTOR OF ACCESSION COUNTRIES BEFORE EU ENLARGEMENT

Basic series and insurance coefficients

Basic series of Insurance in the new EU-10 and averages for the EU-15 for 2002 (see Table 1).

Some General Characteristics of the Insurance Sector in the EU-10

The number of insurance companies declined in the old EU-15 as a result of consolidation, but in the new EU-10 it increased until 1997 due to the underdevelopment of the market. The number of employees in insurance also increased until 1997, then stagnated a couple of years and started to decline only afterwards, due to increased productivity, IT, improved corporate governance. The largest insurance company in Central Europe is PZU from Poland.

The life insurance market is more concentrated and has greater potential for growth in the EU-10 than the market of non-life insurance. Market concentration is slowly decreasing. The importance of the insurance market for foreign investors is growing quickly due to liberalization of entry, introduction of EU solvency criteria and privatization of former state monopolies (CEA, eco, no.18, October 2003).

In the future foreigners will take over insurance companies and domestic ownership share will decline. Former state monopolies still have a dominant position in the insurance sector of half of the EU-10, but they will lose that position when the EU solvency standards need to be fulfilled. The variation in premiums in time is larger in the new than in the old EU member states, the reasons being a lack of economic stability and the effort to catch-up.

The investments of insurance companies are less important in the new than in the old EU member states, partly due to the higher importance of non-life insurance in the new EU-10. Declines in unit-linked products and faster growth of life insurance (economic growth, increasing standard of living, tax relief, new social security system) are leading to faster growth in investments than in premiums lately.

EU-15 vs EU-10

Data on economic strength and the level of development are given in Table 1. They represent a benchmark for the EU-10 development and comparison with the EU-15. In 2002, the old EU-15 had a GDP which was 20-times greater, a population which was 5-times larger and thus the per capita GDP was 4-times higher.

There is a positive correlation between economic and insurance development. In 2002, the EU-15, in comparison to the new EU-10, accumulated 55-times more premiums so that insurance penetration was 3-times higher with a density that was 10-times higher. The amount of investment of the insurance sector was 155-times greater, which means the ratio of investments/premiums was almost 3-times higher or the ratio of insurance investments/GDP (51% compared to 6.6%) was 8-times higher.

The EU-15 countries had 15-times as many insurance companies in 2002, but only 9-times the number of employees, which means about 1/3 fewer employees per insurance company. The share of employees in insurance in total employment was twice as great in the old EU-15 than in the new EU-10 in 2002.

The lag of the new behind the old EU members was even greater at the beginning of the transition. During 10 years of transition (1992-2002) the new EU-10 realized higher growth rates in premiums, premiums per capita as well as investments, even though the average GDP growth was similar in both groups of countries.

The share of life in total insurance premiums is 62.7% in the EU-15, but only 39.2% in the EU-10. In investments the comparable shares are: 81.1% against 61.7%. Higher maturity of life insurance in the EU-15 is indicated by the combined ratios: 100% in the old EU-15, 50% in the new EU-10.

Relation within the EU-10 Group and the Position of Slovenia

Differences among new EU-10 Member States are significant regarding economic power and size. According to GDP per capita calculated with official exchange rates Slovenia lags behind only Cyprus and achieved 50% of the EU-15 average in 2002. With the PPP taken into account Slovenia achieves 70% of the EU-15 average.

In insurance penetration Slovenia shares, with a coefficient 0.051, first place among the new EU-10 together with Cyprus. In life insurance penetration Slovenia is the 7th, while in non-life it is first by far.

In insurance density Slovenia was second to Cyprus in 2002 with € 622 gross premium per capita, which is only 28.5% of the average for the old EU-15. In life insurance, Slovenia was third, in non-life it is first among the 10 new EU Member States.

Regarding harmonization with the insurance legislation of the EU Acquis, in June 2003 Slovenia belonged to the six among 10 new member states with the highest degree of fulfillment. Lagging behind were Estonia, Hungary, Slovakia and the furthest behind was Lithuania.[1]

Slovenia shares the first place with Poland in average GDP growth rate in the period 1992-2002 (Poland lagged behind in 2003). It was much higher than the average growth in the old EU-15 helping Slovenia to catch up a little. In premiums and premiums per capita Slovenia exceeded the average EU-10 growth during the observation period (and thus the EU-15 growth rate as well), but growth in insurance investment was below average in Slovenia. Slovenia was third in average growth of premiums (second in life, fourth in non-life), but only seventh in growth in insurance investments due to the use of profits for structural rehabilitation of the insurance sector.

In terms of insurance penetration, Slovenia ties with Cyprus for the 1st place and achieves 57% of the EU15 average.

In share of life in total premiums Slovenia was only seventh among the EU-10. In the share of life investment in total insurance investments with 38.5% it was only eighth.

In absolute number of insurance companies at the end of 2002, Slovenia was second last among the new EU-10 with 14 units, but the country shares fourth place regarding dynamism of their growth in the 1992-2002 period. During that period the number of insurance companies declined in the EU-15 by 8% and the number of insurance employees by 5%, while these measures increased by 60% and 72% respectively in the EU-10. This is an indication of the maturity of the insurance sector in the EU-15 and the underdevelopment of the sector in the EU-10. Slovenia doubled the number of insurance companies and increased the number of employees by 73% which gives it third and the fourth place among EU-10.

The share of insurance companies in majority domestic ownership (only number) declined in the 10-year observation period among the EU-10 from 67% to 54% (much slower than in the banking sector due to delays in restructuring). Only in three countries, The Czech Republic, Malta and Cyprus, domestic share has actually increased during 1992-2002. In the percentage of insurance companies in domestic hands Slovenia was only third among the EU-10 with 78.5%. Lithuania and The Czech Republic had larger shares with 100% and 83% respectively, but they have decreased that share since 2002 while Slovenia has not. Insurance lags behind banking in both legislation and actual restructuring of companies.

Poland had the largest absolute amount of premiums among EU-10 (not surprising if the size of the country is taken into account). The Slovenian share was 4.8% in life and 10.8% in non-life insurance in 2002.

In market concentration, measured by the share of the five largest insurance companies in total premiums (K5) Slovenia was far above the average of the EU-10 (94.3% to 83.4% in non-life, 87.4% to 85.2% in life insurance). The country has the most concentrated non-life insurance market and the seventh most concentrated life insurance market. Market concentration increased among the EU-10 and in Slovenia during the 1997-2002 period.

The crucial indicator of labour productivity is the amount of premiums per insurance employee. It was € 951 thousand on average among the EU-15, € 159 thousand among the EU-10 and € 239 thousand in Slovenia (second place among all the EU-10 despite the small size of the country).

[1] More about that in Štiblar, (2004).

With a 2.6% share of employment in the insurance sector among all employed persons Slovenia holds second place to Hungary, but it is even above the average for the old EU-15.

In the share of insurance investment (€ 1738 million, out of it € 944 million in life insurance) and their growth in 1992-2002 (3.7 times) Slovenia holds fourth place among the EU-10. Its growth is only 56% of the growth of the EU-10, but exceeds the average growth rate of the EU-15 by 1/3. The investment to premium ratio was 2 for the EU-10, 5 for the EU-15, but only 1.4 for Slovenia (only Estonia and Slovakia were worse).

The investment fund-to-GDP ratio was 51% for the EU-15, only 6.6% for the EU-10, but 7.1% for Slovenia.

The life insurance payments to premiums ratio was unusually high for Slovenia in 2002. At 278% it was far above all EU-10 countries (average 50%) and also above the 100% average for the EU-15. It must be a consequence of changes in the methodology of measurement. Increased standards together with the reform of obligatory insurance has increased demand for life insurance in the EU-10, while tax incentives increase the competition in the form of entrance of foreign insurance companies.

The 39 million tolars in administrative expenses account for 13.8% of life insurance premiums in Slovenia, which is below the average for the EU-10 (15%), but it is still the fourth largest share.

In elements of non-life insurance the combined ratio for motor vehicle insurance for the EU-10 average was 103.1%, for Slovenia 103.8%. In health insurance this ratio was 101.4% for the EU-10, only 97.2% for Slovenia.

In total non-life premiums Slovenia has by far the highest share of health insurance among all the EU-10 countries (due to additional health insurance added to this group). By penetration ratio for real estate Slovenia holds first place among the EU-10 with 0.006, together with The Czech Republic and Hungary. In health insurance premiums per capita Slovenia significantly exceeds all other EU-10 members with € 195 (average is only € 11).

In the share of motor vehicle insurance in GDP Slovenia holds first place among the EU-10 with 0.0144 (compared to 0.0113), related to the higher standard of living as indicated by more cars per 100 inhabitants.

In 2002, the insurance companies in Slovenia were larger than the average of the EU-10: by premiums (€ 88.7 milllion is 79% above average for the EU-10, only Poland has more) and by employees (317) Slovenia exceeds by 20% the average for the EU-10. While in premiums Slovenia's number is only 49% of the EU-15 average, for employees it is 193% of the EU-15 number.

With 2.6% of Slovenia's workforce in the insurance sector, it is the second largest employer.

How much does Slovenia exceed the EU-10 and how much does it lag behind the EU-15?

What are the special characteristics of insurance in Slovenia compared to the other EU-10?

– a higher share of non-life insurance (due to included additional health insurance),

– above average penetration and density ratio,

– faster than average growth of insurance premiums but not investment in 1992-2002,

– above average size of insurance companies by premiums and employees,

– far above average share of insurance companies in domestic majority ownership,

– above average concentration of market in both forms of insurance,

– above average labour productivity in the insurance sector,

– below average share of insurance investment and their growth,

– higher than average payouts for life insurance and below average administrative expenses,

– above average combined ratio for motor vehicle insurance and below average for health insurance, with its share in non-life insurance unusually high,

– above average share of property insurance relative to GDP and even more life insurance per capita.

How much was Slovenia lagging behind the averages for the EU-15 in 2002?

In comparison with the averages for the old EU-15, Slovenia was lagging in most indicators in 2002. The benchmark for comparison is 0.26% share of Slovenia's GDP in the EU-15 GDP, 0.53% share of population and thus achievement of 50% of EU-15 GDP p.c..

By the size of collected premiums Slovenia reached only 0.06% of the EU-15 in 1992, but already a 0.15% share in 2002, still only half of the share reached in GDP. In the number of insurance companies Slovenia reached 0.014% of the EU-15 in 1992, but 0.31% in 2002, a result of their 2.2-time faster growth in Slovenia than in the EU-15. The number of employees in insurance in Slovenia represented only a 0.33% share of the EU-15 in 1992, but in 2002 already a 0.48% share, which is close to the share in inhabitants.

Investment funds of Slovenia's insurance sector represented only 0.28% of the EU-15 in 1992, but in 2002 already a 0.33% share, a consequence of faster growth in Slovenia by 1/3. In investment-to-premium ratio Slovenia reached only 24.3% of the EU-15, in insurance investment-to-GDP only 13.6% of the EU-15 in 2002.

In penetration Slovenia reached 57% of the EU-15 ratio, in density ratio even half less, 28.5%, both in comparison to the 50% share in GDP per capita.

In the transition period 1992-2002 Slovenia had 2.8-times faster GDP growth rate on average than of the EU-15. Within that, life premiums grew 2.9-times faster, non-life premiums 3.4-times faster, per capita premium grew 2-times faster, but insurance investment growth was only 80% of the EU-15 average (low profits, more structural rehabilitation).

The share of life insurance in total premiums was only 33.7% in Slovenia, but 62.7% in the EU-15 in 2002; the share of life investment in total investments was only 38.5% in Slovenia, but 81.1% in the EU-15.

In 2002 Slovenia achieved only 25% of the productivity of the EU-15 (premium per employee in insurance), but held a 7.5% higher share of employment in the insurance sector to total employment. In terms of premiums Slovenia's average sized insurance company was half that of the EU-15, in terms of employee numbers it was twice the average EU-15 number. In life insurance with a combined ratio of 287%, Slovenia far exceeded the 100% ratio of the EU-15.

The Situation in Individual New EU-10 Member Countries (evaluation of Swiss-Re, 2003)

CYPRUS: It is not a transition market, but is already similar to the markets of the EU-15. The level of competition is sufficient as is the degree of penetration. Due to small size, this is a less important market for FDI.

THE CZECH REPUBLIC: It is a relatively small market with the potential of growth second to Poland. The state monopoly was privatized in 2001. A decline in the number of insurance companies can be expected together with newcomers from abroad, especially in the field of life insurance. Fulfillment of new solvency requirements will require only 2.8% additional capital.

ESTONIA: Accession to the EU will increase the competitive pressures in all Baltic states, where insurance is currently less developed than in other accession countries adjusted to the EU environment. Consolidation of the insurance sector started in 1998. Among the three Baltic states, Estonia leads in premiums and in GDP. Non-life insurance has an oligopolistic structure with a 93.5% share in foreign ownership. Introduction of private pension insurance will accelerate life insurance. The Baltic states have a shortage of capital in insurance, which will cause problems in meeting the new solvency requirements. They will have to consolidate or allow acquisitions by foreign insurance companies.

HUNGARY: Among all the transition countries, foreign insurance companies were first to enter this market. The normative adjustment and liberalization of the sector happened already at the beginning of 1990s. With a high degree of competition and normative stability the Hungarian insurance sector is the best prepared for EU membership. Therefore EU accession and strict solvency requirements will not cause changes as insurance companies are already 90% in foreign ownership and foreigners will finance re-capitalization. With a decreasing technical interest rate at the end of 2002 the supervisory agency regulated the problem of lower returns on life insurance policies.

During the transition period from 1992 to 2002, Slovenia's GDP growth rate outpaced the EU15 average economic growth 2.8 times.

LITHUANIA: The contry is less prepared for EU accession in the insurance sector, despite the fact that some foreign companies have already entered the market, with a 50% acquisition of the former monopoly among other things. A lack of additional capital for solvency will lead to consolidation by foreign acquisitions in the future.

LATVIA: It is second to Estonia in the size of insurance (€170 million in premiums in 2002). There are only a few foreign companies in the market, but the insurance sector is growing twice as fast as the average for all EU-10 (8% against 4% annually). Legislation and solvency are close to meeting the EU standards.

MALTA: Similar to Cyprus, the insurance market is not that of a transition one, but closer to the old EU-15. Insurance penetration is high, but the market is less important due to its small size.

POLAND: The Polish market represents around 50% of the total EU-10 market. It is still controlled by the former state monopoly PZU with a 51% share in non-life and life insurance; 55% of PZU is still in state ownership. The second by size is the all-European insurance company Eureko with a 30% share. The new solvency requirements may cause a problem for domestic insurance companies, as 1.5% of additional capital is needed. While non-life insurance is prevalent, a greater potential is in life insurance, which can count on 38 million inhabitants, when the standard of living increases.

SLOVENIA: A relatively high standard of living is one of the reasons for the rapid development and spread of insurance. Despite the relatively smaller presence of foreigners in the market the problem of solvency will not arise. Legislation is harmonized with the EU. Slovenia has a high penetration of non-life insurance, but the lowest penetration of life insurance among all accessing countries.

SLOVAKIA: By development level and potential for growth it is fourth among the EU-10, behind Slovenia, The Czech Republic and Poland. German Allianz AG took over first place in the market from the former state monopoly in 2002. Competition will decrease the number of non-life insurance companies, but foreigners will come with accession to the EU.

Correlation: intensity and the sign of relation among insurance indicators

The correlation analysis indicates only the intensity and sign of the relation between the individual insur-

Table 2: Correlation matrix

	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19
1. compf	1	.62	–.19	.29	.13	–.25	.18	–.43	–.14	.58	.07	–.18	.07	–.11	.53	.32	–.02	.37	.30
2. avgerbdp		1	.30	.91	.78	–.14	–.22	–.47	–.50	.25	–.50	–.64	.49	.32	–.05	–.24	–.10	.02	–.15
3. avgerinv			1	.36	.32	.61	–.36	.06	–.52	.09	–.32	–.13	.42	.01	–.37	–.52	.16	–.05	–.39
4. avgerprem				1	.89	–.20	–.34	–.46	–.52	.06	–.61	–.67	.64	.41	–.24	–.46	–.27	–.25	–.31
5. avgerprpop					1	–.09	–.35	–.24	–.41	–.23	–.63	–.62	.48	.65	–.40	–.46	–.08	–.33	–.37
6. bdp02						1	–.26	.43	–.32	.15	–.03	.17	–.29	.17	–.37	–.11	.71	.15	–.26
7. bdppop							1	–.15	.78	.45	.84	.65	.05	–.47	.76	.89	.02	.78	.98
8. emplcomp								1	.35	–.41	–.21	–.08	–.59	.41	–.55	–.10	.73	–.34	–.20
9. emplpop									1	–.01	.56	.44	–.22	–.14	.35	.66	.18	.29	.72
10. harmon										1	.52	.43	.28	–.44	.70	.48	.08	.72	.50
11. invbdp											1	.92	–.05	–.68	.82	.82	–.03	.81	.82
12. invprem												1	–.01	–.60	.63	.60	.01	.65	.59
13. k5l													1	–.17	.20	–.30	–.57	–.01	–.01
14. k5nl														1	–.71	–.38	.46	–.54	–.48
15. krcompf															1	.72	–.31	.75	.78
16. prembdp																1	.22	.84	.93
17. premcomp																	1	.16	.04
18. premempl																		1	.83
19. prempop																			1

Source: data for individual countries from ECA Report, 2003

ance variables in the group of EU-10, but not the direction of impact, which is subject to regression analysis later.

The absolute value of correlation coefficient r above 0.5 means a strong correlation, between 0.3 and 0.5 moderate correlation, while below 0.3 indicates that the relation is not statistically significant (there are namely only 10 observations in cross country analysis).

The correlation analysis in Table 2 gives simple correlation coefficients for 19 basic insurance indicators for the new EU-10 Member States. They are used for interpretation of basic rules of inter-relation existent among the EU-10 countries (to be compared with the experience of Slovenia). They also mean one of the foundations for specification of the regression analysis in the next step of quantitative analysis.

The share of insurance companies in domestic ownership

It is represented by two variables:

1. The share of insurance companies in domestic ownership in 2002 COMPF is:

a) strongly positively corelated with:

– faster growth of GDP in the transition period 1992-2002,

– greater harmonization of legislation with the acquis in the accession country,

– increase of the share of domestic ownership in 1992-2002 period;

b) it is weakly positive correlated with:

– insurance penetration,

– insurance density,

– labour productivity in the insurance sector,

– growth of premiums in the transition period;

2. Coefficient of growth of domestic ownership in insurance during 1992-2002 is:

a) strongly positively correlated with:

– growth of domestic ownership of insurance in the transition period,

– economic development of the country,

– harmonization of state legislation with the acquis,

– the share of insurance investment in GDP and with regard to premiums,

– higher insurance penetration,

– higher insurance density,

– productivity in the insurance sector;

b) weakly positively correlated with:

higher share of employment in insurance in total employment in country;

c) strongly negative correlated with:

– the average size of insurance by number of employees

– the larger market concentration in non-life insurance,

d) weakly negatively correlated with:

– growth of premiums and investment per capita in the transition period,

– the size of GDP,

– the average size of insurance company by premiums;

The average growth of insurance indicators during the 1992–2002 period

It is represented with three variables plus GDP (a benchmark):

1. The growth of insurance investment is

a) strongly positively correlated with:

– the size of GDP in the country

b) weakly positively correlated with:

– growth of GDP,

– growth of premiums and premiums per capita,

– market concentration in life insurance

c) strongly negatively correlated with:

– the share of employment in insurance in total employment,

– insurance penetration,

d) weakly negatively correlated with:

– economic development

– the share of investment in GDP,

– insurance density,

– growth of domestic share in insurance companies,

2. and **3.** Growth of premiums and premiums per capita, is:

a) strongly positively correlated with:

– growth of GDP,

– concentration in life and non-life insurance,

b) weakly positively correlated with:

– growth of insurance investment,

c) strongly positively correlated with:

– the share of insurance employment in total employment,
– the share of insurance investment in GDP and in premiums,
– concentration in life and non-life insurance market
d) weakly negatively correlated with:
– the country's economic development,
– the average size of insurance companies by number of employees,
– insurance penetration and density,
– productivity in the insurance sector,
– growth of domestic ownership in insurance.

Economic power and country development

1. The economic power of a country is positively correlated with the average size of insurance companies by size and number of employees (economies of scale) and with insurance investment growth.

2. Development of a country (pGDP p.c.) is positively correlated with the share of employees in insurance, ratio of insurance investment to GDP, harmonization of legislation, increase in domestic ownership of insurance, with harmonization of legislation, growth of domestic insurance, with penetration and density insurance coefficients and with productivity in the insurance sector.

It is weakly negatively related to the growth of premiums and investment in insurance and to market concentration in non-life insurance.

3. The average rate of economic growth in 1992-2002 is strongly positively correlated with the share of insurance in domestic ownership, growth of premiums and premiums per capita, market concentration in life insurance. It is weakly positively related to the growth of insurance investment and market concentration in non-life insurance.

Growth of GDP in the transition period is strongly negatively correlated with the size of insurance by number of employees, the share of employees in insurance and the ratio of insurance investment to GDP and to premiums.

The size of insurance companies

1. The number of employees in an insurance company is
a) strongly negatively correlated with :
– the size of premiums per insurance company,
b) weakly positively correlated with:
– market concentration in non-life insurance,
c) strongly negatively correlated with:
– market concentration in life insurance,
– growth of domestic share of insurance companies,

Development of a country is positively correlated with the share of employees in insurance.

d) weakly negatively correlated with:
– growth of the share of domestic insurance companies,
– growth of premiums and GDP,
– harmonization of legislation with the Acquis,
– labour productivity in the insurance sector.

2. The amount of premium per insurance company is:
a) strongly positively related to:
– economic power of country,
– the size of an insurance company by number of employees;
b) weakly positively correlated with:
– market concentration in non-life insurance,
c) strongly negatively correlated with:
– market concentration in life insurance,
d) weakly negatively correlated with:
– growth of the share of domestic ownership of insurance and with the growth of premiums

The share of employment in insurance to total employment is:

a) Strongly positively correlated with:
– economic development,
– the size of insurance investment to GDP or to premiums,
– penetration coefficient,
– density coefficient;
b) weakly positively correlated with:
– employees per insurance company,
– labour productivity in the insurance sector,
– growth of domestic ownership of insurance;
c) strongly negative correlated with:
– growth of GDP and premiums;
d) weakly negatively correlated with:
– growth of premiums per capita,
– economic power of a country.

Harmonization of a country's legislation with the Acquis is:

a) Strongly positively correlated with:
– the share of domestic ownership of insurance and its growth,
– insurance investment to GDP and to premiums,
– penetration,
– density,
– labour productivity of insurance,
– economic development;
b) weakly negatively correlated with:
– the size of an insurance company by number of employees,
– market concentration in non-life insurance.

Insurance investment

The ratio of insurance investment to GDP or to premiums is:
a) strongly positively related to:
– economic development,
– the share of employment in the insurance sector in total employment
– harmonization,
– growth of domestic ownership of insurance companies,

– penetration coefficient,
– insurance density,
– labour productivity in the insurance sector

b) strongly negatively correlated with:
– GDP growth,
– growth of premiums per capita,
– market concentration in non-life insurance

Market concentration

a) For life insurance it is positively correlated with growth of premiums, investment, GDP and premiums per capita (in non-life only with growth of premiums); in non-life insurance with the size of insurance companies by employees and by premiums.

b) It is negatively correlated in life insurance with the size of insurance companies, in non-life with the economic development, harmonization, insurance investment, growth of domestic ownership in insurance, labour productivity in the insurance sector, penetration and density.

Insurance penetration coefficient (premiums to GDP) is:

a) Positively correlated with economic development, the share of insurance employment in total employment, harmonization, insurance investment, growth of domestic ownership of insurance, productivity of the insurance sector and its density.

b) negatively correlated with the growth of investment and premiums as well as with market concentration in both, life and non-life insurance

Insurance density (premiums per capita) is

a) Strongly positively correlated with:
– economic development,
– the share of employees in insurance,
– harmonization of legislation,
– insurance investment,
– growth of domestic ownership in insurance,
– productivity in the insurance sector,
– insurance penetration:

b) It is weakly negatively correlated with:
– growth of premiums and insurance investment,
– concentration in non-life insurance.

Labour productivity in insurance (premiums per employee) is:

a) Strongly positively correlated with
– economic development,
– harmonization of legislation,
– insurance investment,
– growth and the share of domestic ownership of insurance,
– insurance penetration and insurance density.

b) weakly negatively correlated with:
– growth of premiums in the observation period,
– the size of insurance companies by number of employees.

Summary of correlation analysis

The following general rules are obtained from the correlation analysis:

– a larger share of insurance in domestic ownership is positively correlated with insurance development (insurance culture, productivity, domestic ownership) and with greater harmonization of legislation with the EU acquis;

– a larger share of foreign ownership is positively correlated with the larger country size, (larger market potential), larger size of insurance companies, lower level of insurance development, and higher market concentration in the country;

– accession countries with lower insurance development and with higher foreign presence were able to catch-up with the more developed countries in the 1992-2002 period through premium growth;

– in the EU-10 with insurance companies of a larger average size, market concentration is higher; they belong to larger countries with lower insurance development and therefore faster premium growth.

REGRESSION: IMPACT DETERMINANTS FOR INSURANCE IN EU-10

Identification of determinants for insurance in the EU-10

A summary of regression analysis is given in table 3. Statistical indicators include values of regression constant a and regression coefficients b, their statistics of statistical

Table 3: Regression analysis

Y	=	a	+	b1	.	X1	+	b2	.	X2	R2	F
(1) prembdp	=	.0101	+	.0000031	*	bdppop					.802	.32.5
		(2.29)		(5.70)								
(2) prembdp	=	- . 022	+	.0000026	*	bdppop	+	.0042	*	harmon	.844	18.9
		(-.92)		(4.33)				(1.36)				
(3) prempop	=	–302.1	+	0.067	*	bdppop	+	112.5	*	compf	.980	176.1
		(–4.18)		(14.9)				(1.86)				
(4) prempop	=	–341.	+	0.053	*	bdppop	+	105.1	*	compf + 4267. * prembdp	.993	287.2
		(–7.1)		(10.1)				(2.69)		(3.30)		
(5) k5l	=	95.1	–	.139	*	premcomp					.332	3.48
		(22.2)		(–1.86)								
(6) k5nl	=	68.89	–	17.7	*	krcompf	+	2.79	*	avgerprpop	.666	5.99
		(3.79)		(–2.07)				(1.71)				
(7) compf	=	1.62	+	0.118	*	avgergdp	–	0.156	*	harmon	.816	15.5
		(3.02)		(5.10)				(–2.48)				
(8) krcompf	=	0.466	+	0.0000523	*	bdppop	–	.723	*	emplcomp	.722	9.08
		(2.24)		(3.13)				(–2.72)				
(9) premcomp	=	11.15	+	.000268	*	bdp02	+	62.4	*	emplcomp	.744	10.2
		(1.16)		(2.23)				(2.47)				
(10) emplcomp	=	.514	–	.163	*	pop02	+	.0000031	*	bdp02 – .0025 * prempl	.830	9.8
		(3.87)		(–4.11)				(4.44)		(–3.29)		
(11) prememapl	=	.0517	+	3228.2	*	prembdp	+	73.05	*	krcompf	.734	9.67
		(.001)		(2.40)				(1.83)				
(12) invbdp	=	.0917	+	.00000764	*	bdppop	–	.0010	*	k5nl	.818	13.4
		(1.64)		(3.39)				(–1.84)				
(13) emplpop	=	.653	+	.000327	*	bdppop	–	.00895	*	premempl	.653	28.3
		(2.43)		(7.11)				(–3.90)				
(14) avgerprem	=	11.12	+	.854	*	avgergdp	–	126.28	*	prembdp	.646	6.39
		(3.95)		(2.18)				(–2.11)				
(15) avgerprempop	=	.664	+	.729	*	avgerbdp	+	.0708	*	k5nl	.665	10.9
		(.27)		(3.15)				(2.24)				

significance (in brackets below the regression coefficients), determination coefficients R2 and F-statistics for signification of the total regression equation. Only 10 observations are available in the cross section analysis for the 10 new EU Member States. The resented equations presented are statistically significant by all criteria.

The interpretation (substance) includes evaluation of the direction and strengths of impact of independent variables X on dependent variables Y, of which the variability should be explained. Independent variables are tested for multicollinearity, while there is no need for an autocorrelation test in the cross section analysis.

The best estimated regression equations are presented in Table3 and enable the following interpretation.

An increase in the GDP per capita of €1000 increases the penetration coefficient by 3 tenths of a percentage point, while without any GDP the penetration coefficient would still be 1% (equation 1). In addition, improving harmonization by 1 point (the number indicates the best fit to the acquis, held also by Slovenia) contributes to a higher penetration by 0.4 percentage points (2).

Increasing GDP per capita by € 1000 increases the density coefficient by € 67 (3), while a 1% higher share of domestic ownership increases the density coefficient by € 1.1 (3). A 1 percentage point higher penetration coefficient increases the density coefficient by € 42.6 (4).

Increasing the average size of an insurance company by € 100 million decreases the market concentration coefficient in the country by 13 percentage points (5). Increased domestic ownership of insurance companies by 1% during 1992-2002 decreased the market concentration coefficient in non-life insurance by 0.177 percentage points, while a 1 percentage point higher average yearly growth in density decreases market concentration by 2.79 percentage points (6).

A 1 percentage point higher average GDP growth rate in 1992-2002 gives 11.8% higher domestic ownership share. Higher harmonization of insurance legislation decreases domestic ownership by 15.6% (7).

The size of an insurance company measured by premiums positively depends on the size of the economy (measured with GDP) and the average number of employees in the insurance company.

There are more employees per insurance company in countries with a larger GDP, lower number of inhabitants and lower labour productivity in the insurance sector (10).

Productivity of insurers is positively dependent on penetration and the growth in share of domestic ownership of insurance companies (11).

The share of insurance investment in GDP is positively dependent on GDP per capita in the country and negatively dependent on market concentration in non-life insurance (12).

The share of employed in insurance among all employed people depends positively on the GDP per capita, but negatively on the productivity of insurance employees (13).

The average growth of premiums in the EU-10 during 1992-2002 is positively influenced by GDP growth, negatively by the penetration coefficient in 2002 (catching-up) (14).

The average growth of premium per capita in accession countries in 1992-2002 is positively influenced by average GDP growth and by higher market concentration in non-life insurance (15).

How much does Slovenia differ from the general rules of EU-10 behavior?

On the basis of estimated regression equations the estimated values for dependent variables were calculated for Slovenia and then their difference from the actual values for Slovenia added. Differences indicate direction and intensity of Slovenia's difference from the general rules for the EU-10. The existence of these residuals shows that besides specified explanatory variables for insurance indicators some other forces determine the behavior of the Slovene insurance sector, which differs from the general rules of EU-10.

The results in Table 4 show that the majority of indicators (with the exception of the average size of an insurance company) do not differ significantly for Slovenia from the general rules for the EU-10.

Insurance penetration (1,2) is insignificantly higher in Slovenia, as would come from its level of GDP per capita and a high degree of legislation harmonization, which is due

Table 4: Difference of Slovene insurance indicators from the general rules for EU-10

Dependent variable	Actual value – Y	Estimated value – Y estimated	= Residual = e
penetration:			
(1) PREMBDP	0.051	0.0482	+.0028
(2) PREMBDP	0.051	0.0478	+.0033
density			
(3) PREMPOP	622	611.3	+10.7
(4) PREMPOP	622	611.9	+10.1
market concentration			
(5) K5L	87.4	82.77	+4.63
(6) K5NL	94.3	82.8	+11.5
domestic ownership			
(7) COMPF	.786	.924	–.138
(8) KRCOMPF	917	.842	+ .075
size of insurance companies			
(9) PREMCOMP	88.7	40.9	+47.8
(10) EMPLCOMP	.371	.224	147
productivity			
(11) PREMEMPL	238.7	231.7	+ 7.0
insurance investments			
(12) INVBDP	.0707	.0700	+.0007
employment in insurance			
(13) EMPLPOP	2.6	2.5	+.1
growth of premiums and premiums per capita			
(14) AVGERPREM	10.8	9.8	+1.0
(15) AVGERPREMPOP	10.8	11.7	– .9

Source of calculations: regression equations in table 3 to additional factors, such as insurance culture.

The insurance density (3,4,) is around 2% higher than what would come from the level of GDP per capita, the share of domestic ownership of insurance companies and the insurance penetration. Insurance culture could again be the reason.

Market concentration in Slovenia is higher on both markets (5,6), in life insurance by 4.6 percentage points, in non-life insurance by 11.5 percentage points, as would follow from the size of insurance companies, and the share of domestic ownership in the growth of premiums per capita. Among the possible reasons could be the lag in privatization of Triglav insurance and Sava re-insurance company or the less attractive small local market.

It is interesting that by number of insurance companies in majority domestic ownership Slovenia is even 13.6% below the share which would come out with regard to the high GDP per capita and the high degree of legislation harmonization with the acquis. The difference could be explained by the fact that foreign insurance companies are very small in Slovenia, so that the foreign share in premiums would give a number closer to the general rule. On the contrary, the increase in the share of foreign insurance companies in the transition period in Slovenia was even 7.5% lower than would come out from its economic development and average number of employees in an insurance company (equation 8). Among the explanations could be gradualism in liberalization of entry to the market and the small size of the country.

Slovene insurance companies are significantly larger by both average premium and number of employees (by € 47.8 million or 147 employees) than the size determined for the EU-10 by the economic power of country, size of the population and labour productivity in the insurance sector (9, 10). The size is related to the dominant position of Triglav insurance company and its privatization; but it can become an advantage in competitive affirmation at home and abroad (economies of scale).

In 2002, labour productivity in the Slovene insurance sector was 3% above the value which would come out from estimated rules for the EU-10 with regard to the penetration coefficient and the share of domestic ownership as determinants (11). Among other determinants explaining the difference might be better corporate governance and supervision in Slovenia.

In insurance investment compared to GDP, Slovenia does not differ from the rule for the EU-10, determined by the economic development and market concentration (12).

The share of employees in insurance among all employed in Slovenia (13) is one tenth.

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VZAJEMNA
zdravstvena zavarovalnica, d.v.z.
za prostovoljno zdravstveno zavarovanje
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Membership of Slovenia in the European Union and Insurance Supervision

*Jurij Gorišek**

MEMBERSHIP OF SLOVENIA IN THE EUROPEAN UNION AND INSURANCE SUPERVISION

This paper has been prepared to show as briefly as possible the complexity of preparations and the adopted insurance legislation both in the EU and in Slovenia. Namely, the insurance legislation is the very basis for the operational action of supervisory institutions, and for performance of measures of supervision against the offending subjects within each country, as well as by the European Commission against the Member States violating the directives adopted in the insurance field.

In recent years, the EU regulatory framework has responded quickly to the increasingly complex relations on the European financial markets – at first, the directives adopted in the field regulated only supervision of individual companies, then supervision of one-sector groups, which has finally developed into the inter-sectoral supervision of financial conglomerates. In parallel and also taking into account the experience of the banking solvency system "Basel 2", for several years now new bases have been developed to revise and update the European insurance solvency regime – "Solvency 2". The goal of all these amendments and new directives is to ensure security of policyholders through better financial risks management and transparency of financial statements.

Membership of the European Union (hereafter, the EU) brings Slovenia a number of rights as well as considerable obligations in all financial areas and their regulations, including the insurance industry and pension insurance. The EU regulates this area in an increasingly strict and uniform manner by having adopted always new and amended directives for 30 years (in total 40 directives). A number of very complex directives are currently being prepared and are about to be adopted in the EU and in the national proceedings which will impose new tasks on the supervisory bodies of the EU Member States and will inevitably require their professionally more sophisticated qualification and harmonization. Numerous international and EU institutions, as well as committees and specialized sub-committees have been set up to deal with problems and to train the leading supervisors. Over the last year, individual experts from the Insurance Supervision Agency (hereafter: Agency) started to attend these groups.

Slovenia started converging its insurance legislation with the *acquis* relatively late – in the mid-90s. Following the adoption of the Insurance Company Act, the Office of Insurance Supervision was established in spring 1995 at the Ministry of Finance (hereinafter the MF), much later than the Banking Supervision Department which is still twice as strong in terms of headcount than the Agency despite the fact that it oversees the same number of large entities covering a much wider range of insurance areas than banking supervisors. No wonder that during the last four years the Agency and the MF (as legislator) stepped up effort to

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implement financial regulations and supervisory practices in insurance committed to meeting requirements and time-limits set by the EU Commission, and thus financially strengthen Slovenia's insurance industry in line with the EU standards.

However, as regards the ownership structure, Slovenia's insurance sector stands out of the new Member States by being "its own boss" and creating its own development strategy for managing fast growing long-term insurance provisions, savings and guarantee funds. Needless to say that Slovenia should act carefully and not violate the European rules referring to fair competition, single financial market and consumer protection.

OBJECTIVES OF INSURANCE LEGISLATION AND SUPERVISION IN THE EU

In the developed world, the insurance industry and pension insurance are a financial source of long-term financial funds, accounting for two thirds of capital market operations. On the one hand, this means filling up the insurance reserves with the savings of the population, and to some extent, property premiums of legal entities and free (own) capital formation of the insurance undertakings. On the other hand, this means an investment basis for economic development, thereby employing the active population. Both areas are a foundation of economic environment financial stability.

The insurance process is based on expectations and performance of the insurance contract concluded between the policyholder and the insurance undertaking. The objective of the insurance legislation with all relevant secondary legislative acts is to protect the policyholder in terms of reserves which the insurance undertakings fulfil, with which the policyholder concluded the contract, and which must always and at any moment be solvent.

Policyholder protection is designed in particular for natural persons or families who are not familiar with the complexity and (un)reliability of the insurance financial statements (the EU advocates full-scope disclosure and publishing financial statements) or with small print and notes in the insurance policies. Based on the EU directives and domestic legislation, supervision must contain such risks and restore balance. This is the only way to preserve and foster trust in the insurance system, thereby maintaining the economic capacities and safeguarding savings of the population.

On the other end of the insurance process there are investing and increasing provisions and own funds as the aims of the insurance industry. These activities have a significant impact on the financial stability of a country and determine their stability. Therefore strict principles and rules of prudent and safe investment and asset-liability matching must be observed in investing insurance funds.

In line with the above aspects and significance of financial services for the national economy, the EU Commission adopted in 1999 (Köln) the Financial Services Action Plan - FSAP until 2005. The Plan refers to regulating the EU single internal financial market and instituting rules of deliberate operations and supervision for which the EU has already adopted or is currently preparing numerous directives. The EU internal insurance market frameworks are determined by the following:

– three generations of directives, divided into life and non-life insurances;

– the right of establishment and freedom to provide services;

– single passport, reciprocity in mutual recognition and common minimum standards.

Financial Services Committee (FSC), responsible for the »political control« and support to the ECOFIN Council and the EU Commission, plays an important role in adopting directives . The latest FSC report (April 2004) refers to analysing the achieved situation of the EU financial strategy and defining priority tasks of future work, including the insurance sector. Since May 2004, Slovenia has participated fully in discussing these issues in different committees and working groups.

This section can briefly be concluded with a definition that the main objectives of the EU insurance legislation and supervision are to secure the safety of policyholders and their trust in the financial system institutions, financial stability and integrity, competition and market availability of financial services, and consequently, stable economic development and employment in the EU. Accepting and implementing the EU directives are of the utmost significance for the European economic environment, as they are for Slovenia as its part. In any other event, measures are taken by the EU Commission and an application is submitted at the European Court of Justice (ECJ) in Luxembourg, as is already a well established practice among the EU Member States.

DEVELOPMENT AND SITUATION OF EU INSURANCE LEGISLATION

Significant Directives to Date

To achieve the said objectives, the EU prepared and adopted new insurance directives, commencing (if we exclude the 64/225/EEC directive on reinsurance freedom in the EEC) with the 73/239/EEC directive (First Non-life Directive) on property insurance, followed by the life insurance directive, then with the next generation of directives for both insurance groups, motor insurance directives, accounting insurance directive, etc.

The EU legal framework was gradually constructed to implement the so-called »solo« supervision of insurance undertakings while the individual areas, as already mentioned, were upgraded with several generations of directives. Of particular importance are three generations of life and non-life insurance directives which took 20 years to finalise the definition of freedom to provide insurance services in the EU – a single European passport and mutual recognition while observing minimum standards. These directives also defined elements for calculating the solvency margin of insurance undertakings setting minimum standards for technical provisions, own funds and investment policy. Together with provisions of the insurance accounting directive, a basis for comparable financial statements and supervision across the EU was set out.

In recent years, the EU institutions have invigorated effort to draft and adopt new insurance directives and modify and amend those already in place,. Working groups, subcommittees and committees composed of experts from all EU Member States from the supervisory bodies and the insurance industry"discuss the issues together with the organisations representing consumers and professional associations (actuaries, auditors, accountants), etc...

Directives on Insurance Groups and Financial Conglomerates

One line of the new directives elaborated on the solo supervision of the insurance group (Insurance Group Directive – 98/78/EC) upgrading to supervision of financial conglomerates (Financial Conglomerate Directive – 2002/87/EC) with the principal aim of correctly demonstrating, without double counting, the solvency position of these groups/conglomerates, risk concentration in groups/conglomerates and possible perilous risk transfers between group members or conglomerates. It should be noted that within the implementation of the insurance group supervision, which often extends across the borders of one of the EU Member States, the Helsinki Protocol of supervisory multilateral cooperation of EU Member States, Norway, Iceland and Liechtenstein was adopted. This means that the EU25 no longer have to conclude Memorandums of Understanding (MOU) because with accession to the EU or EEA (the European Economic Area) they can obtain supervisory information under the above-mentioned The Helsinki Protocol Working Group (HPWG)headed by the President of the Norwegian supervisory authority, has been created with the aim to facilitate this cooperation.

However, those countries whose insurance groups or financial conglomerates have operations outside the EU must continue to conclude MOUs with the third countries if they wish to supervise the whole group in terms of reporting (data and information exchange) and carry out on-site inspections. Thus the Agency will have to sign MOUs with Croatia, Bosnia & Herzegovina, Serbia and Montenegro, etc. so that it can successfully carry out consolidated supervision in a group or a financial conglomerate, including the Zavarovalnica Triglav, d. d. insurance company.

The Financial Conglomerate Directive (2002/87/EC) provides a better basis for greater financial stability and institutes a higher degree of protection for depositors, policyholders and investors. Furthermore, it boosts the supervision effectiveness and coordination of supervisory proceedings across financial sectors and state borders. Furthermore, it sets new, more consistent requirements for solvency margins, prevents »multiple gearing and downstreaming« of the capital of the parent financial companies and the abuse of their financial inflows from bond issues for supervised subsidiary's equity capital (banks, insurance undertakings, etc.) which brings about the so-called excessive leveraging. The directive also sets restrictions and requirements as to risk concentration at the conglomerate level and the same as with transactions between conglomerate members. The requirements as to specialized expertise, reputation and experience of the board members and in relation to internal supervision systems in the conglomerate have been made stricter. Due to involvement of different supervisory authorities in the home country and other countries (supervision of subsidiaries), the rules of responsibility are imposed on the chief supervisor – coordinator and the rules of cooperation and information exchange among supervisors, including those from non-EU countries. In compliance with more elaborate requirements, the directive supplements and amends the rules in the directives for homogenous – single-sector financial groups.

Directive with regard to insurance intermediation was adopted to provide better protection to consumers – insured persons.

The deadline to launch the financial conglomerate directive in the internal legislation of all EU 25 Member States is 11 August 2004, so there are thorough and intensive preparations of the MF Act under way in Slovenia, in cooperation with all three supervisory authorities.

These indications and the fact that among 70 financial conglomerates in the EU, at least one of them will be from Slovenia (with an insurance undertaking at the top position), we can foresee and assess the new role, obligations, powers and responsibilities of the Agency within the EU in the future.

Fourth Motor Insurance Directive

The Fourth Motor Insurance Directive (2000/26/EC) requires that the insurance undertaking appoints a damage adjuster in every EU Member State who must react no later than in three months otherwise the insurance undertaking and the national institution will face a penalty for compensation which must be established in every Member State, together with the information centre. For example, disregarding the time limit to institute the directive in the state's legal order in 2003 triggered EU Commission proceedings against Ireland and Luxembourg.

Directive on Insurance Mediation

For better consumer protection, in our case insurance undertakings, the insurance mediation directive was adopted (Insurance Mediation Directive – 2002/92/EC) which provides that the mediators must be registered (licensed), possess adequate knowledge, be of good repute (fit and proper), have valid liability insurance for 1 to 1.5 million euros, and always provide the policyholders with prior written information.

Directive on Winding up Insurance Companies

As a result of missed deadlines to implement the Winding up Directive (2001/17/EC) in connection with the policyholder protection, the EU Commission instigated proceedings against Belgium, France, Luxembourg, the Netherlands, Finland, Sweden and the United Kingdom. Similarly, the EU Commission filed an application on the basis of Article 226 of the agreement against Belgium, Greece, the Netherlands, Finland and the United Kingdom, for not adopting the directive on solvency of life (2002/12/EC and 2002/83/EC) and non-life (2002/13/EC) insurance undertakings in time (by 20 September 2003).

Some Directives in the Process of Adoption or in Preparation

Fifth Motor Insurance Directive

The Fifth Motor Insurance Directive, on which the Member States reached political consensus in November 2003 and which will have its second reading in the EU Parliament after the summer, provides minimum cover of 1 million euros for a victim of a road accident, plus an option of 5 million EUR for the accident, and 1 million euros for material damage after the transitional five-year period.

Pension Funds Directive

The IORP Directive (Directive 2003/41/EC) must be transposed to national legislation by 23 September 2005. Its aim is to protect funds and transactions of pension (capital) insurance which already cover 25 per cent of the EU workforce and have funds of 2,500 billion euros (29 percent of the EU GDP). This should also enable expansion of safe and effective pan-European pension funds.

The directive includes two significant principles, i.e. no interference in the organisation of national pension systems and respect for national differences with a high degree of protection for policyholders; it concurrently observes four objectives:

- security of the system safety;
- accessibility and efficiency;
- cross-border membership;
- competitiveness and comparability among providers.

The directive also defines investment policy rules of pension funds, the supervision area, etc.

In February 2004, the Committee of the European Insurance and Occupational Pensions Supervisors of the EU Member States – CEIOPS established a special working group to deal with pension insurance, problems with implementation of the directive and the expansion of cooperation protocol in this sphere. Two colleagues, who are certified actuaries of the Agency, are also members of the group.

The main spheres of the new directives currently being prepared by the EU sub-committees and working groups are as follows:

- Solvency II project
- reinsurance
- guarantee schemes
- e-marketing of insurance services
- accounting
- equality between the sexes

Solvency II Project

The most comprehensive and already initiated EU insurance project is Solvency II. A special sub-committee of the Insurance Committee EU was established and are already handing over most of their work (as they say: »the locus and focus of work«) to the working groups within CEIOPS. The objective of the project is to change the existing solvency system in the EU and to prepare a more appropriate system at two levels. At Level, now finished, the members and offices of the EU Commission examined a number of spheres, such as the RBC systems (»risk based capital«), experience of the Basel capital requirement rules, the application of internal control models, the development and implementation of the report and Lamfalussy recommendations, links between financial reports and audit statement etc., in order to set up a framework for the future European solvency system. Level 2is to follow, that is the preparation and adoption of directives.

The fundamental objective of the Solvency II project is to prepare higher standards for individual risks based on a three pillar structure, board members' eligibility and internal control risks, better harmonization between legislation and the EU state supervisors, including the avoidance of inter-sector arbitrating during supervision. Within this groundwork the standards for calculation of technical provisions and minimum target capital, which will depend on the risks taken over or covered by an insurance company, will be amended.

In order to achieve the objectives of the project, work on some other concurrent spheres has intensified, such as application of the international insurance accounting standards, (preparation of) the reinsurance rules, the previously mentioned reserves standards (the EU Commission counts on the active support of the IAA/Group Consultatif Actuariel European – for the actuary principles and training), solvency, etc., which will lead to preparation or performance of special directives.

Within the three pillars of the Solvency II project, the CEIOPS established five working groups in February 2004:

- pillar 1 – life and separate non-life insurances,
- pillar 2 – supervision review,
- pillar 3 – a group for disclosures and accounting as well as a special group for inter-sector harmonization.

The Agency nominated its experts (10) in all three working groups which is one of the best foundations for efficiently transposing the directives into Slovenian supervisory practice and liaisoning with other supervisors in the EU.

It is planned to submit the directive proposal to the EU Commission in 2005.

Proposal for the Directive for Reinsurance Companies Supervision

After the last meeting of the IC Reinsurance Subcommittee at the end of October 2003, the EU Commission offices prepared a proposal for a directive for reinsurance company supervision. In these months, the EU Commission will submit a formal proposal to the EU Parliament and to the Council of Europe to institute a legislative procedure. Adoption of the directive is of great interest to the G7 Group, the World Bank, IAIS and OECD as there is no harmonized framework to implement prudential reinsurance supervision in the EU.

The groundwork of the directive is the already developed rules for direct insurances and also the newly extended and supplemented IAIS principles from October 2003 (28) which, as opposed to those existing previously (October 2000) (17), include assessment of insurance legislation alongside reinsurance supervision.

Adoption of a special reinsurance legal framework will consequently call for amendments to the directives with regard to life and non-life insurance, insurance groups and financial conglomerates, as well as directives on winding up insurance undertakings. There are proposals that the directive includes increased solvency requirements for reinsurance companies as their operations are exposed to greater risks.

Introduction of Guarantee Schemes in the Insurance Industry

As opposed to banking and investment funds, in the EU insurance industry there are no compulsory guarantee schemes – a safety net for policyholders in the event of liquidation and bankruptcy of an insurance undertaking. In fact this is *ex ante* or *ex post* fund formation to protect the policyholders, especially in compulsory and life insurances. The IC – EU working group was established to study this area. Some states actually have such funds/ schemes and some do not. According to a survey (Market / 2528 / 03), most EU Member States believe that the benefit of the guarantee schemes would be greater than their costs. Some states, however, have refrained from replying until the first draft of the directive is issued in autumn 2004. It is clear that in different states there are different problems in initiating warranties in terms of the market structure and in terms of the level of guarantee, insolvency threat, etc.

Accounting

The EU has already issued five directives for accounting in insurance undertakings, the most exhaustive one in 1991 and the latest amendment in 2003. Extensive discussions are being held to update accounting insurance standards and to amend valuation by implementin fair value principles in liabilities and assets. At the end of March this year, the International Accounting Standards Board – IASB adopted

Directive on retirement provision has to be transposed to national legislation by 23 September 2005.

the IFRS 4 standard for insurance contracts - as a temporary Phase 1 until a permanent standard of this kind is prepared. IASB had already adopted an amended a version of the international standards IAS 32 and 39 and others which are to be used from 1 January 2005. These are being studied by the European Financial Reporting Advisory Group (EFRAG), while in June the motion will be submitted to the EU Commission. The activity includes other committees, such as the CEIOPS working group for accounting and disclosures involving the participation of one of the Agency's experts. The amended IASB insurance standards will inevitably have an impact on the Solvency II project. It is expected that Phase 2 – adoption of the overall insurance standard – will take place after 2007.

Equality between the Sexes

In the insurance area there is another interesting regulation being prepared -»equality between the sexes« in a special directive already prepared (COM 2003 – 657 final). The important provision is the prohibition against calculating different insurance premiums and associated financial services with regard to gender. It would be applicable only to new contracts, following a long period after the directive has come into effect. Then the EU Member States concerned should issue renewed mortality tables and update them regularly. This will of course mean a small »revolution« in liability and life insurances to which a number of the EU Member States are opposed.

To finish this rough review of the EU legislation, let us repeat the assessments provided by Mr Olivier Fliche on behalf of the EU Commission at the 17th Conference of the European Supervisors, held on 22 May 2003 in Ljubljana: *»the EU expects that the FSAP plan realization for the period 1999–2005 in the area of financial services integration on the internal market will increase the GDP by 1.1 percent, employment by 0.5 percent, and reduce costs of own funds/equity capital and corporate bonds by 0.5 and 0.4 percent respectively in ten years.«*

DEVELOPMENT OF INSURANCE LEGISLATION AND INSURANCE SUPERVISION IN SLOVENIA

Period up to the Year 2000

We can see that EU membership also brings Slovenia considerable obligations in the insurance industry. The initial preparation in Slovenia was the adoption of the Insurance Companies Act (Official Gazette, No. 64/94) and establishment of the Office of the Insurance Supervision at the MF (15/3/1995). The first such act in independent Slovenia and one of the last in the acceding states established foundations (particularly on the basis of the first and partly the second generation of the main EU insurance directives) on which the Office of the Insurance Supervision commenced with a small number of staff and meagre resources the fight to improve the gloomy situation on the Slovenian insurance market.

After a loss (write-offs) of about 40 percent of our insurers' funds, the state of the Slovenian insurance industry over the period of five years can be described as follows:

– completely insolvent with insufficient reserves in all insurance undertakings;

– monopolised market with more than 60 percent in the hands of the largest insurance company;

– the ownership bill still pending after three years of adopting and enacting two relevant acts in the Constitutional Court with an extreme danger of unjust appropriation of the majority ownership of the insurance undertakings and thus the majority management of insurance funds. In two insurance groups, funds are getting close to two billion euros;

– shifting funds, even life premiums, into payments for motor insurance and other claims ;

– lack of interest of foreign insurance companies and investors to help improve the Slovenian market;

– indebtedness (illiquidity) of some insurance companies;

– "creative" accounting (underprovisionong) to enable distribution of profit and payment of dividends

– pyramid – network selling of life insurances with an extremely high (up to 50 percent) drop of contracts in three years after conclusion;

– wide-spread ignorance about the complexity of insurance company accounts and the market except in (some) insurance undertakings and insurance brokers, etc.

Given the insurance sector characteristics here stated, the first Slovenian insurance act was only a »remote« regulation target we strived for and it was achievable only over a longer period of time. Alternatively, we could have instigated a string of bankruptcies of insurance undertakings without any protection for policyholders, even for the insurance class of compulsory motor insurances. This, however, was neither the intention nor the aim of the newly established supervisory body.

The Office of the Insurance Supervision started to »break new ground« as it was compelled not only to revitalise the state of the Slovenian insurance market, but also to train the staff of the insurance supervisor and to initiate relevant education (Master's degree in insurance finance and actuarial studies). Intensive capital increase was initiated and is still being implemented (in total about 30) as required by the Supervisor. Concurrently, other violations are being remedied, first of all of life insurances and reserves, then other technical provisions, the deficit in own capital, the deficit in consolidated balance sheets and so forth. The active and positive role of the Sava Reinsurance company as well as some large corporate or financial companies on the coast should be specially emphasized. Without them these activities would not have been viable and the trust of Slovenian policyholders and savers in our financial system would have been heavily eroded and damaged. In this way, however, the insurance industry did not have to join bankruptcies in other financial sectors.

Apart from the investments write-offs, two more spheres considerably contributed to extremely »difficult« position in our insurance industry in the 90s. The first were the insurance guarantees given to domestic and foreign banks for loans granted to natural persons and entrepreneurs. Such loan insurances caused the insurance companies to incur tens of millions of D-marks in loss so that at the end there would be only one insurance company left in the market with huge insurance amounts of bank loans. The IMF and the World Bank have warned us for the last four years (also in their last FSAP Update Report) of a possible systemic risk (economic recession – unemployment and debtors going bust) due to such and other (deposits and ownership) interdependences between Slovenian banks and insurance undertakings, and emphasized the need that such vast credit insurance contracts should be handled by a specialist insurance company.

The second sphere relates to motor insurance with previously frozen premiums which, in four years, incurred a cumulative loss amounting to one-year gross premiums (about 20 billion tolars by 1999). At the initiative of the Office of the Insurance Supervision, the problems in this sphere were analysed by actuaries of the Government Actuary Department – GAD from the United Kingdom. Despite the unfavourable findings of the GAD analyses and regular reports to the Ministry of Finance and the former Ministry of Economic Affairs, it took the Office three years to persuade the Ministry to allow premiums in this insurance class to rise, and to eliminate adverse circumstances with disastrous effects on the balance sheets of insurers, as life premiums were also being used to settle motor insurance claims, making a laughing stock out of the law which was particularly meant to protect life insurance policyholders in the event of a bankruptcy – Article 86.

Period after the Year 2000

With a limited number of staff – eight employees and inadequate statutory opportunity to take measures - the Office of the Insurance Supervision got a new Insurance Act (ZZavar, Official Gazette of the RS, No. 13/00) which established the Insurance Supervision Agency on 1 June 2000. With 364 articles, the new Act instituted many new elements from all the then existing generations of life and non-life insurance directives, covering cooperation with EU supervisory bodies, the insurance group supervision, the capital adequacy calculation of individual insurance undertakings and insurance groups, regular reporting to the Agency, its rights, status and obligations and decision-making procedures; it eliminated inequality in respect of the national treatment, preliminary offers of domestic reinsurance, preliminary approvals of insurance conditions, with the exception of compulsory motor-vehicle liability insurance and supplementary health insurance, and allowed the Agency to approve insurance undertakings investments abroad, etc.

A bit long-winded in parts (mutual insurance companies, the Agency's proceedings), the Act, however, did not solve some important issues, such as:

– it did not solve the problem of equalisation schemes in supplementary health insurances which are the largest insurance class in Slovenia therefore a large legislative, thus supervisory, vacuum continues to persist in this area;

– it retained the option that one auditing house can be engaged in the same insurance undertaking indefinitely;

– it did not decrease possible excessive growth of equalisation provisions, thereby causing a bogus slide in financial results and the capital adequacy of an insurance undertakings. This is also partly true for nuclear risks reserves, bonus, etc; all this has had the result that the solvency and financial situation in our insurance enterprises cannot be on an equal insurance-accounting bases with others in Europe;

– the Head of the Agency was not granted the same protection in the event of a non-culpable dismissal as was introduced for members of the Council of Experts;

– the Act continued to »indefinitely« allow composite insurance companies of which Slovenia now has the highest number. This does not provide transparency and necessary »fire walls« between the life and non-life insurance groups, still allowed in the same legal entity under the same management board,

– it did not provide a suitable place for the register of insurance agents and insurance brokers.

The Act (Article 108) solved quite well the problems of dual capital counting, not only in the insurance sector but also in the broader financial group (conglomerate) for which some of the EU Member States (e.g. Italy) still do not have a suitable statutory regulation. In their case, this will be regulated by the financial conglomerate directive, once it is introduced in practice.

Since its adoption in 2000, the Act was significantly amended in March 2002 (ZZavar – A) withregard to restriction of equalisation provisions to 12 insurance classes and a breakdown of the surplus of equalisation provisions in the amount of about 23 billion tolars or their consideration when calculating capital adequacy. These legislative innovations were

connected with internal ownership (share) procedures in the largest insurance undertaking,

and indirectly with lengthy procedures and problems »when adopting the property» acts. Then

the largest insurance undertaking »feverishly resisted« the reduction of equalisation

provisions and their transformation into capital. This year their wishes were just the opposite

and were considered in the IA (ZZavar – B) as to inclusion of additional equalisation

Unlike banks and investment funds, insurance guarantee schemes are not mandatory in the EU.

rprovisions (about SIT 9 billion) in the solvency (equity) capital (once the taxes have been

paid and the limit of the additional capital considered). We can also add that our insurance tax

system will need to be amended again particularly due to peculiarity of forming technical

provisions. The need has already been demonstrated in said changes in the equalisation provisions.

We should take in consideration that in the Directives 2002/12/EC and 2002/13/EC the equalisation provisions are not included in the stated elements of the disposable minimum capital but only as reserves. Tendencies of the EU and particularly of the IASB are that the equalisation provisions, as a part of insurance and technical provisions, are to be suspended and replaced with suitable reserves from net profit.

The present balance of total equalisation provisions in the Slovenian insurance industry amounts to almost 40 billion tolars. If it was included in capital, the current total solvency of our insurance undertakings would be doubled. In the USA and the EU most insurance undertakings in solvency reach between 200 and 300 percent level of regulatory capital. We can see that in accounting and financial terms we have caused ourselves damage and aggravated our international advantage, but all this is of course connected with the fortunately unsuccessful huge ownership appetite.

As for the supervisory institution, only the IA (Zzavar) promulgated in 2000 opened the door for its development. The Agency which got its own budget and recruited many experienced staff in one year, strengthened its position both internally and externally, and adopted more than 20 secondary legislation acts in time. Ayear ago, after eight years of carrying out supervision, it could not attract a lawyer with a bar examination. It was not before the overall climate changed and the situation in the largest insurance company was back to normal, that the Agency succeeded in employing several lawyers with a bar examination and fill in four certified actuary posts in early 2003.

The Agency has worked hard on image-building at home and abroad, particularly within the IAIS, the EU conferences, seminars, committees and other meetings. Its high-calibre experts prepare three to five papers for these meetings every year often coupled with a preliminary survey covering various professional areas (depending on the topic of the meeting). The International Monetary Fund (IMF), the World Bank (WB) and EU supervisors have assessed the work of insurance supervision and the legislation four times in recent years. All these activities gradually improve our qualification of the supervision to successfly implement EU insurance legislation or the legal insurance order in practice.

On 7 May, the Act amending the Insurance Act (hereafter: IA-B) came into effect. The amendments include provisions of already adopted insurance directives mandatory for Slovenia after EU accession. A single insurance passport took effect for all the EU Member States with regard to authorisation, supervision, compulsory information exchange, single investment market, etc... For the Agency all this means an extensive additional responsibility and requires relevant qualifications. The IA-B eliminates most of the said shortcomings. It does not, however, solve all the problems of supplementary health insurances that will have to be solved by other acts. The composite insurance undertakings also remain under one legal umbrella with their peculiarities and the dangers of life and non-life insurances. The IA-B imposes even more obligations on the Agency, especially in the international and inter-sector area while its internal and external operations (measures) are essentially unchanged.

In short, there are intensive preparations going on in Slovenia to transpose the Financial Conglomerate Directive to the national legislation by adopting the Financial Conglomerates Act by mid-August this year. We believe to be the first to promulgate such an act, and we hope it will be a solution to an extremely complex and as yet unfinished theme.

As said, at the level of EU directives and internal legislation, we should consider, particularly in this Act, the needs to harmonise and amend the sector financial acts for the insurance industry, banking industry and securities market. There are special committees and working groups at the EU and IAIS level to study the legislation and supervisory proceedings for financial conglomerates whose members are also on the staff of the Agency. Every EU Member State is liable to inform the EU working bodies, on the basis of surveys, of any possible occurrence or existence of financial conglomerates in its financial market. These reports will provide lists (registers) of the main coordinators of supervision and their locations for all EU financial conglomerates so that eventually it will be absolutely clear where the centre of harmonised supervisory information will be or the proceedings related to individual financial conglomerates. In Slovenia it is expected that there will be at least one such coordinator.

ORGANISATION OF SUPERVISORY AUTHORITIES IN THE EU AND IN SLOVENIA, THEIR MISSION AND COOPERATION

On 5 November 2003, the European Commission adopted a package of decisions (IP/03/1507) so that EU Member States can respond more rapidly and more efficiently to current financial sector developments. The objective of these decisions is to accelerate the legislative processes at the EU level and help with consistent application of common rules in all 25 EU Member States. The package consists of one directive and six decisions of the European Commission which are to set up an up-to-date and clear decision-making structure for financial services and improve cooperation among the regulators and supervisors. In the banking and insurance sector (pension funds included) this in fact, sets up the same structure of committees and proceedings, as has been in practice for the securities market and investment funds since 2002 (UCITS), in order to secure better financial integration as well as protection for customers and investors. On 31 March 2004, the EU Parliament endorsed the Lamfalussy Extension Directive in its first reading and it will probably become final this summer.

In November 2003 three national supervisory committees were established within the same package, i.e. for banks – CEBS (Committee of European Banking Supervisors), for insurance and pension funds – CEIOPS (Committee of European Insurance and Occupational Pensions Supervisors) and for the securities market – including investment funds – CESR (Committee of European Securities Regulators). Early this year, the ECOFIN Council decided to have their permanent registered offices in London, Frankfurt and Paris. Thus the deliberative body of the European insurance and pension supervisors is moving from Paris to Frankfurt where everything is ready to initiate activities in the CEIOPS Secretariat, also regarding the venue of at least two regular annual meetings, working groups and others. The third annual meeting of representatives of the supervisory bodies of the CEIOPS Member States will be »hosted«, i.e. by a particular EU Member State. The January meeting was held in Paris, the June meeting will be a »transitional« one in Brussels while the regular October meeting will be organised by the Agency in Ljubljana together

IMPORTANT ABBREVIATIONS USED

CEBS	Committee on European Banking Supervisors
CEIOPS	Committee of European Insurance and Occupational Pension Supervisors
CESR	Committee of European Securities Regulators
ECJ	European Court of Justice
ECOFIN	Economic and Financial Affairs Council
EEA	European Economic Area
EFRAG	European Financial Reporting Advisory Group
EU	European Union
FSAP	Financial Services Action Plan
FSC	Financial Services Committee
GAD	Government Actuary Department
GCAE	Group Consultatif Actuariel Evropean
GDP	Gross Domestic Product
HPWG	Helsinki Protocol Working Group
IAA	International Actuarial Association
IAIS	International Association of Insurance Supervision
IAS	International Accounting Standards
IASB	International Accounting Standards Board
IC	Insurance Committee
IFRS	International Financial Reporting Standards
IMF	International Monetary Fond
MOU	Memorandum of Understanding
OECD	Organization for Economic Cooperation and Development
UCITS	Undertakings for collective investment in transferable securities
WB	World Bank

with the CEIOPS Presidium (last year it was held in Athens).

At the January Conference it was decided to discontinue the option of submitting contributions in three languages (English as well as German and French) so that the only working language in conferences and working groups will be English. As said, ten experts from the Agency actively participate in the CEIOPS working group meetings to cooperate and to consult, and to harmonize the initiation of common European regulations, practice and training. This is the only way we can hope that Slovenia will gradually catch up with other supervisors of the Member States and become »equal« in this field.

Furthermore, a discussion on integration of financial supervisors was initiated in the EU within the FSC (Financial Services Committee). The FSC members agreed that a discussion about establishing a Single European Supervisor is premature and that Lamfalussy's three-level process should continue in order to prove its value.

A similar opinion on the (un)suitability of an accelerated merger of the three supervisors in Slovenia was expressed by the IMF and WB representatives in the latest FSAP report in November 2003. They believe that the year 2004 is not suitable for Slovenia as it is filled with key and that it would be much wiser to postpone the amalgamation of the supervisory authorities, prepare adequately and examine all pros and cons. In our opinion, the amalgamation is due to take place in one to three years, given the size of Slovenia, the interconnection and interdependence of financial sectors and emerging financial conglomerates or relevant directives.

It is important to continue and strengthen the current cooperation in all fields among the Slovenian financial supervisory authorities as has been done over the last three years. In the meantime, acquiring knowledge, cooperating in the committees and working groups of the CEIOPS, CEBS and CESR and other institutions (the Basel associations), as well as developing a harmonised information statistical basis, will be an excellent basis for supervisors to join forces at a later date.

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Slovenian Reinsurance and Cross-Border Challenges

*Siniša Lovrinčević**

SLOVENIAN REINSURANCE AND THE CHALLANGES OF INTERNATIONAL BUSINESS OPERATIONS

Right from its beginning, the Slovenian reinsurance industry has aimed at providing economic security as part of international business operations. Slovenia's accession to the EU in May 2004 has opened up more challenges and opportunities. By continued prudence and creative co-ordination of interests among all interest groups involved in the development of the Slovenian reinsurance market, we can attain an adequate level of quality and brilliancy in doing business on an international level. By harmonising financial, human, emotional and social capital, we become stronger within, while by focusing on the custormer, we become stronger on the outside. In keeping focused on basic expertise and skills of our own staff, we can, through the system of knowledge circulation and transfer, develop commitment and promote the socialisation of all vital parts of the organisation. Taking into consideration the new paradigms of contemporary views on reinsurance markets as part of the wider economic system, I believe that the Slovenian reinsurance industry will be able to continue its mission.

Closing thought: I would like to see the development of the Slovenian reinsurance industry through a continuous process of self-questioning with a feeling of self-confidence.

From cradle to grave, day in, day out, the man is exposed to and threatened by all sorts of dangers, hazards and perils. Consequently, he is open to various adverse effects, which may affect him, his loved ones and his property. As we are affected by these negative influences, we feel the need to protect ourselves, to steer clear of treacherous waters or to find shelter if not a safe haven. The modern society we live in, and the business world in which we operate, are largely shaped by techniques and technologies which have been developing at an unprecedented rate and adding to the uncertainty of our existence. In 1991, Slovenia witnessed changes that were to redesign its social, economic and political landscape. The transition to a market economy exposed the Slovenian economy to business deals clinched at a higher rate of uncertainty and risk. At this point insurance comes to the forefront together with reinsurance as a stabilising factor endowing the economy with a dose of security (e.g. non-life corporate insurance, liability insurance), and providing an individual with a “life-line” for his or her daily activities (e.g. life assurance, accident insurance). The very essence of insurance was captured in the definition given by the nestor of the Slovenian insurance business, Jože Boncelj: »Insurance is the creation of economic security by equalizing economic hazards« (Boncelj, 1983). The objective of insurance is to provide an economic safe-heaven; how safe it really is in the face of danger can actually be measured. The need for reinsurance surfaced after the invention of insurance when it ran out of financial strength to level off risks. The simplest definition of reinsurance is

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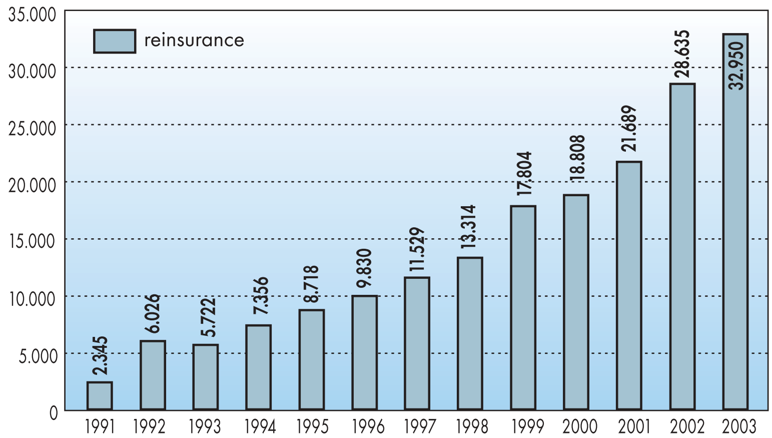
»insurance of insurers«. This type of insurance goes hand in hand with insurance and acts as a (vertical) risk equaliser for insurance undertakings. We can simply state that reinsurance corresponds to insurance. A more elaborate explanation of reinsurance is offered by the Slovenian Insurance Act promulgated in 2000. Article 2 defines that reinsurance is »insurance of the excesses over the level of the own equalling of risk by one insurance undertaking at another insurance undertaking«. Even a quick comparison of the characteristics displayed by the two activities discloses that they are intertwined, mutually dependent and on track leading to the creation of economic security. Insurance and reinsurance fall within the scope of business originated and finalised among people. The business relationship is built upon the mutual trust of all participants in the provision of (re)insurance services. Confidence starts to grow between the insured person and the representative of the insurance undertaking and continues when going one level up to reinsurance (trust shared between the insurer and the re-insurer), and also exists in the international reinsurance market (between the re-insurer and retrocessionaire).

Development of reinsurance in Slovenia

At the beginning of 1973, the Slovenian insurance company Sava took up active reinsurance in addition to insurance activity. It was a cornerstone for the construction of the framework for the development of Slovenian "home-grown" reinsurance. If I sum up the findings made by Flis, the entry of the Slovenian reinsurer into the international business environment back then enabled a broader territorial dispersion of insurances, direct business contact with foreign insurance and reinsurance undertakings, insight into the developments in the international insurance and reinsurance market and acquiring experience and knowledge through additional professional training (Flis, 1995). Three years later, the market share held by Zavarovalnica Sava was already 10.9 per cent of the Yugoslav reinsurance market (Flis, 1995, I. book : 125). The development of reinsurance that followed suit can be divided into several development periods. At this point I will move on to the milestones in the development after the year 1990 when the insurance communities started transformation to public limited companies. It was the time branded by the Law on the Foundations of the Property and Personal Insurance System adopted in 1990. Pursuant to that law, Sava Reinsurance Community was transformed into Pozavarovalnica Sava d.d. (1990) followed by Inter, pozavarovalna družba, d.d. (1991), Pool for the Insurance and Reinsurance of Nuclear Risk GIZ (1994) (Pavliha, 2000). The development of Slovenian (re)insurance focused on putting in place a regulatory framework designed along the lines of the market systems of Western Europe. The purpose of operations carried out by economic entities was to provide (re)insurance, the goal was to make profit. It was followed by the Act on Insurance Companies promulgated in 1994, when the Slovenian insurance converged with the directives of the European Union (Zupančič, 2000). It was when Slovenian insurance entered the period of »market operations, competitive fight and modern insurance supervision« (Bijelič, 1998: 16). As argued by Pavliha, the Act stipulated »mandatory exploitation of domestic reinsurance capacities, a public limited company carrying on insurance business in majority or controlling foreign ownership was not allowed to take up reinsurance business, or establish a reinsurer« (Pavliha, 2000: 326). Later on the third Slovenian reinsurer was incorporated – Triglav Re, d.d. (1998). Insurance contracts concluded by the Slovenian insurance companies until the beginning of 1999, were reinsured at two Slovenian reinsurers – Inter, pozavarovalna družba, d. d., with the head office in Maribor, and Pozavarovalnica Sava, d. d., with the head office in Ljubljana. Both reinsurers accepted risks up to covering the ceiling of their capabilities. The excess of risk was reinsured in the international reinsurance market. As early as in 1999, a feature of the Slovenian reinsurance market was asymmetry and a very small share of life reinsurances in the reinsurance premium written. Reinsurance business used to be dominated by Pozavarovalnica Sava (Sava Re), a heavyweight reinsurer in terms of capital (holding approximately 93 per cent of the market) and also boasting a much longer tradition. In the wake of the incorporation of the reinsurer Triglav Re, d. d., headquartered in Ljubljana, the slices of the reinsurance market were cut differently. Inter, pozavarovalna družba, d.d. was wound up in 2001.

The rise in gross reinsurance premiums written in the Slovenian reinsurance market between 1991 and 2003 is illustrated in Figure 1. We can see right away that the volume of gross reinsurance premiums written, gathered by the Slovenian

Figure 1: Development of gross reinsurance premiums written in the Slovenian reinsurance market between 1991 and 2003 (in millions of tolars)



Source: Slovenian Insurance Association, 2004, Ljubljana.

reinsurers, has been growing since 1991 (the premiums of the reinsurer Triglav Re was already taken into account in 1999).

According to the data compiled by the Slovenian Insurance Association (Statistical Insurance Bulletin 2003), gross premiums written in the Slovenian reinsurance market (reinsurers Sava Re and Triglav Re) totalled 28.6 billion tolars in 2002. The growth rate was twice the rate posted a year earlier. As at 31 December 2002, all reinsurers had 59-strong staff and each employee generated on average 458.339.000 tolars in gross reinsurance premiums written. The share of reinsurance in total direct premiums topped 10.7 per cent in 2002, 1.3 percentage points higher than in 2001. The bulk of reinsurance premiums (7.4 billion tolars) was written to cover fire insurance policies followed by insurance for motor vehicle liability (6.2 billion tolars), other types of non-life insurance ranked third (5.8 billion tolars). In 2002, no extreme loss events were recorded in the Slovenian insurance market. Compensations paid out in the amount of 14.6 billion tolars were 10.2 per cent below the figure posted for the year 2001. The loss result in 2002 was 51 per cent – a record low since 1991.

The liberalisation of reinsurance business was put on track with the most recent reform of Slovenian insurance endorsed under the new Insurance Act adopted in 2000. The Act governs the field of insurance in the Republic of Slovenia providing systematically for compliance with the European legislative framework – *acquis communautaire* and pencils in a new roadmap for development. Furthermore, it exposes Slovenian reinsurers to new challenges posed by international operations and calls for exploring all avenues that will lead to strategic solutions and eventually sharpen their cutting edge.

Are we facing new challenges by doing business in the international reinsurance market

A flash back to the history of the Slovenian reinsurance business shows that from the very beginning it was a line of business honed by international practice. Exchange of experience and knowledge gained by working hand-in-hand with both domestic and foreign business partners has helped to foster prudential principles and caution of the Slovenian reinsurance management when deploying reinsurance instruments. The set objective was clear: to ensure economic security to all users of reinsurance services. Day in, day out, it bears positively on sustained confidence and reputation that alongside human and financial resources are the key elements of Slovenian reinsurance in effort to preserve existing and acquire new business opportunities. The challenges we are facing today in the international environment are also the challenges shaping the development of Slovenian reinsurance.

Globalisation needed in order to cut costs, steady increase in natural catastrophe events, unforeseeable dimensions of terrorist attacks and losses incurred in capital markets are the challenges present in the world reinsurance market. Additional challenges Slovenian reinsurers encounter are market liberalisation and privatisation that calls for identifying appropriate ownership structure. All the aforementioned challenges demand on-going adjustment of reinsurers. Strategically they have already responded in the wake of the catastrophic 11 September 2001 event. Being able to post black figures under technical provision items, applying risk management methods across the »chain of risks«, creation of financial stability and high quality of reinsurance services (adequate scope and cover price) have become a routine in reinsurers' response as they embrace this comprehensive approach driven by the need to control changes that keep popping up (see Pavliha, 2003). This year's full-fledged membership of the Republic of Slovenia of the European Union poses a new question: what will happen to the development of Slovenian reinsurance? As we try to answer the question whether Slovenian reinsurance is prepared for the challenges of the international business co-operation, I hasten to ask another one: is international reinsurance ready for the challenges raised by operating in the »global village« of which Slovenia is a part? I happen to believe that in reinsurance management, preparedness is thought of as a long-term process having no fixed commencement or termination date; no wonder it demands quick response to a change whenever it occurs. Since we are awash in supply and demand we are geared toward achieving the highest possible level of readiness, i.e. responsiveness to market requirements. We keep abreast of new management tools: by asking original questions, we shape the future of our own development and world reinsurance, being aware that hazards do not choose time, victims, or place. Slovenian reinsurance is the key security element of the mosaic of successful economic development of the future.

A couple of thoughts on the strategic placing in the international »high voltage grid«

Western European countries experienced early in the 1980s a relative loss of economic power. Governments of the Member States of the European Community arrived at the conclusion that by taking joint action, they may tackle the problem and the way to do it was by creating a single market (see Hartman, 1995: 9). As observed by Henke, a single insurance market is part of »the general concept of the single European market« and does not feature any specific characteristics in the entire concept of the European integration (Henke, 2000: 26). The fundamental idea and an indispensable basis for making the single European market come true is functioning free movement of goods, people, capital and services. By subscribing to such an approach, the citizens of all Member States would presumably be living in a land of plenty. The expected economic effects of the creation of the internal market should be palpable both in supply and demand. In particular:

– costs are expected to fall and consequently, prices as well;

– plummeting prices will stimulate demand and will have a positive impact on curbing inflation;

– companies will step up activities and make better use of their resources;

– competition will get fiercer creating a self-sustaining circle;

– market integration will encourage creation of new jobs;

– the inflow of foreign investment into the European Union is likely to gain momentum.

We may assume that the effects listed above would not occur simultaneously. The common goal is the scale at which corporate competitiveness can be boosted and the level at which customers are well-off. Nevertheless, we should warn that becoming competitive just through price cuts may appear convenient to users in the short-term, but it may cause the loss of development tendency for innovation and the creation of new services (e.g. the development of alternative risk transfer) (see Krumberger, 2002). By doing so, the Slovenian reinsurers (Sava Re and Triglav Re) are faced with challenges, which include placement on the European Union market and at the same time safekeeping their position in the domestic market. To illustrate the argument, I will take a look at German experience. The first German conclusion was that »selling cross-border insurance is more difficult« than they would have expected (see Henke, 2000: 27). German experience with regard to the single insurance market after 1994 are related to four categories: confidence, products, marketing/selling, legal framework (Table 1):

Table 1: German experience with the internal insurance market after 1994

Category	German experience after 1994
Confidence	Trust in domestic insurance companies is higher as a rule.
Products	The known products are more popular. People are unwilling to trade them for new offers. The problem of acknowledging an insurance service (product) has been identified.
Sales	Sales in the insurance industry is firmly founded on long-term partnerships - this means on domestic insurance companies (there are established social relations already in place). This particularly applies to a market being characterised in the first place by insurance agents rather than insurance brokers, as in the case of the German insurance market.
Legal framework	Selling cross-border insurance is more cumbersome mainly as the result of unfinished harmonisation of the single market in all areas of legislation (e.g.: insurance contract law, tax legislation),

Consequently, the German insurance market has been confronted with the following four challenges (see Henke, 2000: 28):

– the presence of a small number of providers from other European countries;

– a small number of new products of domestic insurance undertakings; new products hardly ever arrive from foreign countries;

– competition growing stronger along with the deregulation of the single market (the requirement to approve prices and insurance terms has been abolished), but only among German insurers;

– a high degree of diversity and complexity of insurance offers, as well as price cuts, have still left clients unconvinced, so they continue to question whether they have been given the best deal possible (e.g. car insurance).

What is then expected from Slovenian reinsurance management? Resorting to a new management paradigm as stated by Nordström and Ridderstrale; »The most important means of production is small, grey, weighs around 1.3 kilos and is called the human brain« (Nordström, Ridderstrale, 2001: 18). Organisations and services associated with them are becoming increasingly similar. The difference has to be found elsewhere. The potential for competitive placement of Slovenian reinsurance is hidden in people, their distinctiveness, the way in which they are managed and directed, and in the art of organising unusual things with ordinary people. Slovenian reinsurance is already integrated into the business »high voltage grid« where the future cannot be predicted any more but it has to be created. Being aware that intangible assets such as trust, brand, reputation, long-term business co-operation, in-house knowledge, ideas, are becoming most valuable, the focus on human resources and knowledge is the hard currency of success. My personal conviction is that by endorsing the vision of »learning people«, Slovenian reinsurance will be creating a competitive edge in the international »global village« of uncertainty. It is of little or no relevance where a reinsurance service comes from; What really matters is who's covered!

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Insurance Against the Consequences of Natural Catastrophes

*Andrej Kocič**

INSURANCE OF NATURAL PERILS

The natural catastrophes have always represented a major threat to lifes and property of humans. Specifically, the list of 20 biggest insurance losses from 1970 to 2003 stresses the prevailing dominance of natural catastrophes, which caused 18 biggest losses from the list. Statistics has showed that the natural catastrophes are most often caused by earthquakes, storms and floods. Therefore, the management of natural perils has always been of the specific importance for the insurance and reinsurance industry. Due to high level of development of non-life insurance products in Slovenia, there are numerous insurance products which include the cover of natural perils, e.g. fire insurance, home content insurance, contractors and erection insurance, business interruption insurance, casco and cargo insurance. It is of the essential importance, that the process of management of natural perils in insurance and reinsurance involves also the insureds (through loss prevention, loss minimization and retention) and the state (especially the land use regulation, building codes, physical measures to protect the infrastructure and favorable tax treatment of natural perils reserves). The innovation in the financial markets has changed the insurance and reinsurance of natural perils, especially throught the development of the alternative risk transfer methods, i.e. cat bonds, cat swaps and contingent capital. This has, however, not happened yet in the Slovenian financial markets.

An important part of insurance protection is protection against the consequences of natural disasters for people and their property. Insured risk which may cause natural disasters are therefore incorporated into various types of insurance. These forms of insurance are also available in Slovenia, where they have been developed in line with insurance and reinsurance practice abroad. It was, in fact, the need for reinsurance against the implications of natural catastrophes that brought about the harmonisation of insurance in Slovenia with the principles applied in other developed insurance markets.

The Devastating Consequences of Natural Catastrophes and Their Impact on Insurance

Insurance terminology defines a natural catastrophe in various ways:

1. A catastrophe is "a loss event resulting in destruction across a wide area or in a limited space, or causing significant damage to property, numerous deaths or injuries, or serious environmental damage". Characteristic of a natural catastrophe is that the loss event is caused by natural phenomena (e.g., storm, flood, earthquake, etc.). (Zanetti, 2004, p. 42)

2. Characteristic of a major natural catastrophe is that it causes damage which the affected area cannot rectify by itself, thus necessitating international aid. As a rule, we speak of natural catastrophes in cases where "thousands of people are killed

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and hundreds of thousands are made homeless, or when a country suffers substantial economic losses in view of the economic circumstances generally prevailing in that country ". (Topics 2000, Natural Catastrophes – The Current Position, 1999, p. 41)

Northridge earthquake which caused a USD 17.3 billion insurance loss in 1994. The most common causes of natural catastrophes are storms[1] (hurricanes, typhoons, winterstorms, tornadoes, etc.), earthquakes and floods.

Long-term trends related to insurance against natural catastrophes are particularly important for insurance companies. Table 2 shows the movement of natural catastrophes, economic and insurance losses, and the share of insurance losses in economic losses by decades from 1950 to 1999. An increase in all observed categories is evident, except for the share of insurance losses during the 1960s and 1970s.

The relative data shown in Table 3 are even more important than the absolute data. We can see that in all of the observed decades insurance losses increased more rapidly than economic losses, in relative terms. At the same time, in all of the observed decades both insurance and economic losses increased more rapidly than the number of natural catastrophes, in relative terms. These movements are very important for insurance companies, as they point to the ever more devastating consequences of natural catastrophes in terms of the economic losses they cause. Of particular importance is the increase in insurance losses, due to which insurance companies are facing new challenges, one of the most important of which is the provision of appropriate capacities.

As emphasised above, the main types of natural catastrophes are storms, floods and earthquakes.

Table 1: 20 Most Costly Insurance Losses from 1970 to 2003

Insurance loss* (in USD m)	Date (start)	Event	Country
21,062	11. 9. 2001	Terrorist attack on WTC, Pentagon and other.	USA
20,900	23. 8. 1992	Hurricane Andrew	USA, Bahamas
17,312	17. 1. 1994	Northridge earthquake	USA
7,598	27. 9. 1991	Typhoon Mireille	Japan
6,441	25. 1. 1990	Winterstorm Daria	France, GB, etc.
6,382	25. 12. 1999	Winterstorm Lothar	France, Switzerland, etc.
6,203	15. 9. 1989	Hurricane Hugo	Puerto Rico, USA, etc.
4,839	15. 10. 1987	Storm and floods	France, GB, etc.
4,476	25. 2. 1990	Winterstorm Vivian	Western and Central Europe
4,445	22. 9. 1999	Typhoon Bart	Japan
3,969	20. 9. 1998	Hurricane Georges	USA, Caribbean
3,261	05. 6. 2001	Tropical storm Allison, torrential rains, heavy flooding	USA
3,205	2. 5. 2003	Thunderstorms, tornadoes, hail	USA
3,100	6. 7. 1988	Explosion on Piper Alpha platform	GB, North Sea
2,973	17. 1. 1995	Great Hanshin earthquake	Japan
2,641	27. 12. 1999	Winterstorm Martin	France, Spain, Switzerland
2,597	10.09. 1999	Hurricane Floyd, heavy downpours, flooding	USA, Bahamas
2,548	6. 8. 2002	Severe floods	Europe
2,526	1. 10. 1995	Hurricane Opal	USA, Mexico
2,288	20. 10. 1991	Forest fires which spread to urban areas, drought	USA

* Benefits based on property insurance and insurance of business interruption. Data do not include benefits based on liability insurance and life insurance. Prices stated are from 2003.
Source: Zanetti et al., 2004, p. 38.

Table 1 shows the 20 largest insurance losses that occurred in the world from 1970 to 2003. The losses are ranked according to the scope of the insurance loss, representing the sum total of the claims from property insurance and business interruption insurance. Eighteen of the 20 losses listed were caused by natural catastrophes, the other two losses being "Mand' Made Cat"– the terrorist attack on WTC, Pentagon, etc. in 2001 (the largest single insurance loss), and the explosion on the Piper Alpha platform in 1988. Among the natural catastrophes, a special place goes to Hurricane Andrew, which caused a USD 20.9 billion insurance loss in 1992, and the

Table 2: Number of Natural Disasters, Economic Losses, Insurance Losses and Share of Insurance Losses in Economic Losses on a Global Scale by Decades from 1950 to 1999

	1950–1959	1960–1969	1970–1979	1980–1989	1990–1999
Total number	20	27	47	63	82
Economic loss (in USD b)	38,5	69,0	124,2	192,9	535,8
Insurance loss (in USD b)	n. p.	6,6	11,3	23,9	98,8
Share of insurance loss in economic loss (%)	–	9,57	9,10	12,39	18,44

n.a. – No data available
- Calculation makes no sense.
Source: Topics 2000, Natural Catastrophes – The Current Position, 1999, p. 43.

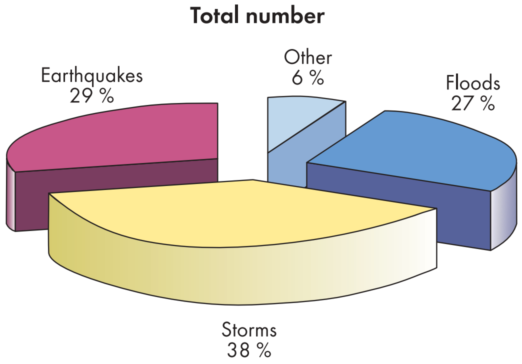
Table 3: Ratio Between the Number of Natural Catastrophes, Economic Losses and Insurance Losses on a Global Scale by Decades from 1950 to 1999

	Ratio			
	1990–1999/ 1980–1989	1990–1999/ 1970–1979	1990–1999/ 1960–1969	1990–1999/ 1950–1959
Total number	1,3	1,7	3,0	4,1
Economic loss	2,8	4,3	7,8	13,9
Insurance loss	4,1	8,7	15,0	–

– Calculation makes no sense.
Source: Topics 2000, Natural Catastrophes – The Current Position, 1999, p. 43.

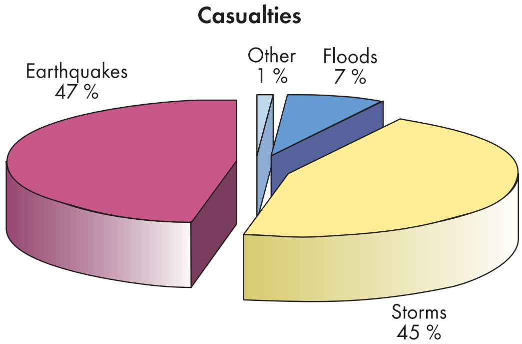
[1] A storm in insurance conditions is defined as a wind speed of at least 17.2 m/s, 62 km/h or of level 8 on the Beaufort scale (Article 5 of General Conditions for Fire Insurance, PG-poz/99-6, Zavarovalnica Triglav, d.d.).

Figure 1: Share of Floods, Storms, Earthquakes and Other Natural Catastrophes in the Total Number of Natural Catastrophes on a Global Scale from 1950 to 1999



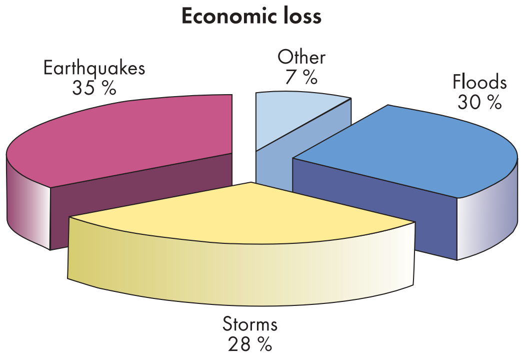
Source: Topics 2000, Natural Catastrophes – The Current Position, 1999, p. 42.

Figure 2: Share of Floods, Storms, Earthquakes and Other Natural Catastrophes in the Total Number of Fatalities on a Global Scale from 1950 to 1999



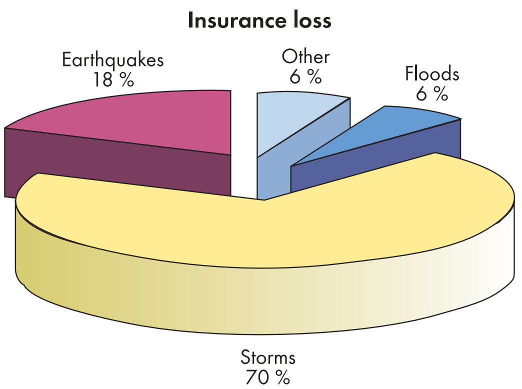
Source: Topics 2000, Natural Catastrophes – The Current Position, 1999, p. 42.

Figure 3: Share of Floods, Storms, Earthquakes and Other Natural Catastrophes in Total Economic Loss on a Global Scale from 1950 to 1999



Source: Topics 2000, Natural Catastrophes – The Current Position, 1999, p. 42.

Figure 4: Share of Floods, Storms, Earthquakes and Other Natural Catastrophes in Total Insurance Loss on a Global Scale from 1950 to 1999



Source: Topics 2000, Natural Catastrophes – The Current Position, 1999, p. 42.

Other types of natural catastrophes include forest fires, frost, drought, etc. Figures 1 to 4 show the shares of the main types of natural catastrophes in the period from 1950 to 1999. As shown in Figure 1, the number of natural catastrophes in the observed period was fairly equally distributed among floods (27%), storms (38%) and earthquakes (29%).

A comparison of the number of fatalities in the second half of the 20th century (total 1.4 million) shows that the two main causes were earthquakes (47%) and storms (45%) (Figure 2).

The main source of economic losses (total USD 960 billion) in the observed period was earthquakes (35%), whilst floods were the source of economic losses in 30% of cases and storms in 28% (Figure 3).

Characteristic of insurance loss (total USD 141 billion) in the observed period was the extremely high share of storms (70%), while the shares of earthquakes (18%) and floods (6%) were substantially lower (Figure 4). The underlying reason for such a high proportion of storms is that storms are often included in the insurance cover of property insurance as an insured peril.

The Necessity of Partner Cooperation

For the successful implementation of insurance against the consequences of natural catastrophes it is imperative that insurance companies, reinsurance companies, governments and insured parties cooperate. All of these partners have obligations,which must be adhered to. The obligations of insurance companies are: the design of special kinds of insurance with clear insurance conditions, setting appropriate insurance premiums, separate accounting, accumulation control of natural catastrophes, preparing instructions for risk transfer, determining the limits of insurance cover (participation of the insured party in the loss, reinsurance), and the design of reserves for natural catastrophes. With regard to insurance against the consequences of natural catastrophes, reinsurance companies must: provide capacities through risk equalisation, counsel insurance companies in determining the size of insurance premiums, carry out accumulation control and limits of obligations (limits of reinsurance cover, retrocession), and offer expert assistance in determining Probable Maximum Loss (PML). The duties of the government are: to prepare standards regarding the use of land and the construction of buildings, to exercise control over the meeting of standard requirements, to implement measures for infrastructure protection (building of dams, retention pools, etc.), and to provide a favourable tax status for reserves for natural catastrophes. The tasks of the fourth partner, the insured parties, are: the implementation of measures for the prevention and minimisation of loss, and participation in loss. (Management of Natural Perils in Property Insurance and Reinsurance, 1999)

Options of Insurance Against the Consequences of Natural Catastrophes

The main types of insurance products offering protection of property against economic consequences resulting from natural catastrophes are:

1. fire insurance
2. computer insurance
3. glass insurance
4. leased equipment insurance
5. fairs and exhibitions insurance
6. home content insurance
7. contractors' insurance
8. erection insurance
9. earthquake insurance
10. insurance against business interruption due to fire
11. insurance of events
12. car casco insurance
13. vessel casco insurance
14. aircraft casco insurance
15. cargo insurance
16. crop insurance
17. animal insurance

In the majority of the insurance types listed above, the insured perils are defined in accordance with the system of named perils, so perils that may cause a natural catastrophe must be expressly stated (e.g., storm, hail, and flood during fire insurance). In types of insurance where the insured perils are defined in line with the system of insurance against all risks, the loss resulting from natural catastrophes is covered if it has not been caused by any expressly excluded perils (e.g., computer insurance).

As defined in item 3, one of the duties of the insured party in insurance against the consequences of natural catastrophes is participation in loss – if this is an integral part of the insurance contract. Participation may be effected in the form of franchise or as percentage participation of the insured party in loss.

As in the majority of property insurance, the probable maximum loss (PML) is also calculated in insurance against the consequences of natural catastrophes. To a large extent, reinsurance companies also cooperate in PML assessment.

In Slovenia insurance coverage against most natural catastrophes preying on us can be arranged.

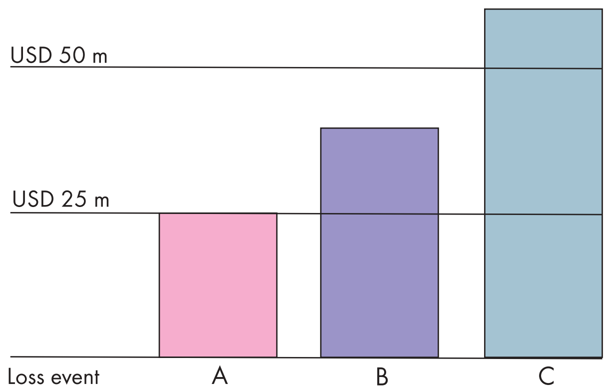
Types of Reinsurance Cover

For reinsuring insurance against the consequences of natural catastrophes, insurance companies obtain both proportional and non-proportional reinsurance cover in the form of both obligatory and facultative reinsurance. The non-proportional excess of loss catastrophe cover (CatXL) is aimed especially at the reinsurance of natural catastrophes. In this insurance type, a priority is set which represents the limit to which the insurer covers the loss in full. An upper limit is also set which represents the upper limit of losses covered by the insurer (up to the priority) and the reinsurer (from the priority to the upper limit). Figure 5 shows an example of a CatXL reinsurance cover operation. Reinsurance cover is expressed as "USD 25 million xs USD 25 million". In the case of a loss event A amounting to USD 25 million, the whole loss is fully covered by the insurer. In loss event B, the loss amounts to USD 40 million; up to USD 25 million of this loss is covered by the insurer, while a further USD 15 million is covered by the reinsurer. In loss event C, the insurer covers the first USD 25 million, the reinsurer covers a further USD 25 million, and the insurer covers the excess over USD 50 million.

Alternative Methods of Insurance Against the Consequences of Natural Catastrophes

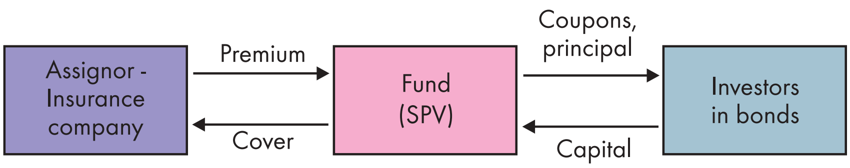
In view of the large scope of economic and insurance damage that can be caused by natural catastrophes, providing sufficient capaci-

Figure 5: Example of a CatXL Reinsurance Cover Operation



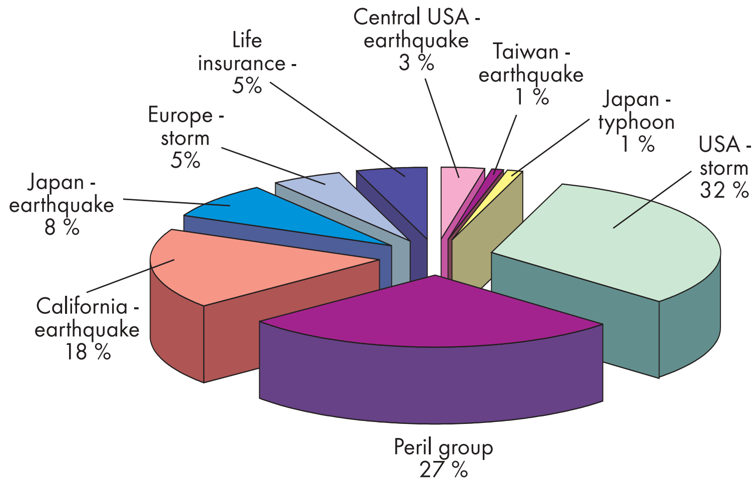
Source: Adapted from Zimmerli, 2003, p. 40.

Figure 6: Example of a catastrophe bond



Source: Belonsky, 1999, p. 5

Figure 8: Structure of Securities Linked to Natural Catastrophes, since 1996, in %

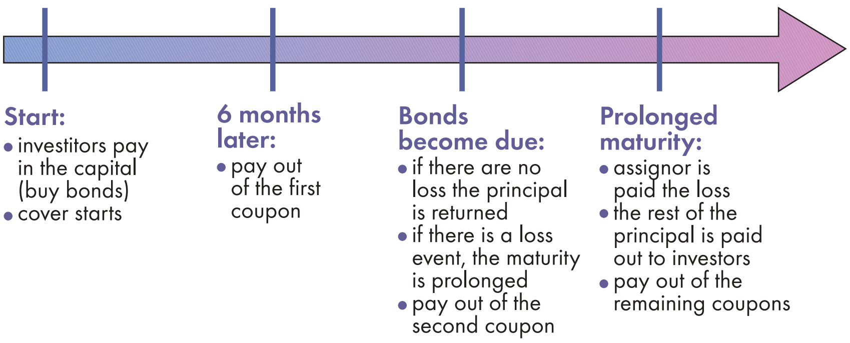


Source: Table 1, Appendix.

ties is of the utmost importance. Therefore, alternative methods of risk transfer in insurance and reinsurance have been developed, which use the capacities of capital markets: contingent capital, securitisation and derivatives. The most important methods, in quantitative terms, are contingent capital and securitisation, especially in the form of catastrophe bonds (cat bonds) and catastrophe swaps (cat swaps). In the area of derivatives, the period from 1995 to 1999 saw trading in PCS options; today, we can trade in weather futures and options on weather futures.

Figure 6 presents the *modus operandi* of a catastrophe bond. Rather than choosing a reinsurance contract, with which an insurance company transfers, for example, earthquake risk to a reinsurance

Figure 7: Catastrophe bond cash flow



Source: Belonsky, 1999, p. 6

company, an insurance company may instead choose to use capital markets. In this case, a special fund has to be established (*Special Purpose Vehicle – SPV*) which issues bonds. Capital intended for the earthquake peril cover is raised with the issue of bonds, giving rise to two relationships - one between the insurance company and the fund, and the other between the fund and the investors. The former is similar to a reinsurance contract, as the insurance company pays the premium and receives cover. In the latter case, however, the investors in the catastrophe bonds are exposed to the risk that the realisation of the insured peril (an earthquake) will result in a decrease of the principal.

Figure 7 shows catastrophe bond-related cash flows. At the beginning, the investors pay in the capital. If there is no loss event, investors have their principal and coupons paid out. If a loss event occurs before the bonds are due, the maturity is prolonged. By the end of the prolonged maturity, investors have the remainder of coupons paid out, and when the bonds are due they also have the rest of the principal paid out.

With securities linked to natural catastrophes, capital market capacities have, until now, mainly been used for insurance against the consequences of natural catastrophes which can affect the most economically developed parts of the world (USA, Japan, Europe, Taiwan), or for multi-peril insurance (Figure 8). The development of the securitisation of catastrophe risks should continue to rise, increasing from the current USD 1 billion per year to USD 10 billion per year by 2010 (Laster and Raturi, 2001).

Insurance Against the Consequences of Natural Catastrophes in Slovenia

In Slovenia, it is possible to take out insurance against the majority of natural catastrophes that are a peril to us: earthquakes, floods, storms, hail, lightning, landslides, and avalanches. Because these are mainly natural catastrophes with a large loss potential, insurance companies also have to provide external risk equalisation, especially in the form of appropriate reinsurance cover. As

APPENDIX

Table 1: Structure of the Securities Market Related to Natural Catastrophes, since 1996

Country/area – insured perils	Value (in USD m)	Share (%)
USA – storm	2,340	31.03
Peril group	1,962	26.01
California – earthquake	1,379	18.28
Japan – earthquake	641	8.50
Europe – storm	414	5.49
Life insurance	400	5.30
Central USA – earthquake	226	3.00
Taiwan – earthquake	100	1.33
Japan – typhoon	80	1.06
Total	7,542	100.00

Source: Zanetti et al., 2004, p. 15.

Table 2: New Issues and Status of Outstanding Securities Related to Natural Catastrophes from 1997 to 2003

Year	New issue (in USD m)	Outstanding (in USD m)
1997	69	714
1998	306	725
1999	305	825
2000	804	1,122
2001	1,454	967
2002	1,853	990
2003	2,204	2,132

Source: Zanetti et al., 2004, p. 15.

elsewhere in the world, the government also has to implement certain measures, relating mainly to the drawing up of legislation and control over its implementation, in order for the insurance against natural catastrophes to be successful. Here we can expect further positive effects because we are obliged to take into consideration the EU *acquis communautaire*. While, on the one hand, we can establish that the system of traditional insurance and reinsurance against the consequences of natural catastrophes in Slovenia is, to a large extent, developed, this is not true of alternative systems. As in other areas, the relatively small size of the Slovene capital market, compared to other countries, should not pose a major problem. Probably a larger obstacle at this point in time is the fact that such securities have not been offered to investors in Slovenia on a scale that would be worth considering.

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Risk Management in Life Assurance

*Darko Medved**

RISK MANAGEMENT IN LIFE ASSURANCE

The article presents an analysis of the risk management system in insurance companies offering life assurance. Six fundamental risk sources are identified: interest rate risk, credit risk, insurance risk, cost risk, operational risk, and general business risk. The article addresses in more detail interest rate, cost and insurance risks as basic risk categories in life assurance operation. For each of the listed risks, basic models for measuring and monitoring are proposed, as well as possible management forms.

The environment in which banks and insurance companies operate in developed economies has changed tremendously in the past few years. This period has been especially marked by low inflation rates and the lowering of interest rates. We have also witnessed a tendency towards great fluctuations in financial markets. Financial institutions are subject to further deregulation and internationalisation of financial intermediation, which increases competitiveness and necessitates increased efficiency of operation. Due to the fall in share values on international markets, more and more banks and insurance companies have been facing the problem of providing adequate solvency. This is why management boards of financial institutions increasingly rely on advanced tools for risk management, as well as developing internal systems of risk analysis aimed at ensuring the long-term stable operation of the company in the competitive environment.

In the future, management boards of insurance companies will have to pay more attention to risk management systems, whereas insurance companies previously dealt mainly with the management of individual risk segments, and less with their common effect on the company's operating results. With the management of individual business processes one does not achieve comprehensive risk management in the company, as the whole risk, especially in financial institutions, is too complex a phenomenon to enable us to separately identify and measure individual risk categories. As established by Guttherman (2002), a high-quality risk management system will be one of the main

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sources of a competitive advantage of insurance companies in the future. Guttherman also highlights the importance of risk management in the development of new products, control and cost management, and financial and operational risk management. Insurance companies, which know how to quantify and manage these basic risk categories will clearly gain a competitive advantage in the market.

The risk management system in insurance companies has a special role. Apart from other general risks similar to those encountered in the majority of business entities, it also underwrites the risks transferred to it through insurance contracts with the company's clients, the insured. In order to better understand the risks that can be transferred to the insurance company with an insurance contract, let us first examine the definition of insurance as an economic activity. In general, there are two definitions of insurance in insurance theory. From the financial point of view, insurance is a financial agreement, which disperses the costs of unexpected losses among the parties to the agreement (Dorfman, 1994). This is fundamentally the definition that was used by Boncej (1983). According to this definition, insurance includes the transfer of potential losses to the insurance pool. The insurance system distributes the costs of losses by collecting an insurance premium from every participant (insured) in the system. In exchange for the insurance premium paid, the insurer commits himself to paying for losses in the case of an insurance event, as defined in advance. According to the legal definition (Dorfman, 1994), insurance is a contractual agreement between the contractual parties whereby one party takes over the obligation to cover the loss incurred by the other party. In such a case, the insurer is the party that takes over the obligation to pay for the insurred loss, while the insured is the party whose loss gives a rise to obligation. In general, the rule applies that the insurance company insures those risks which are sufficiently dispersed and whose frequency follows the rule of economies of scale. Such risks can be described and measured with probability models, enabling the insurance company to implement appropriate control and exposure management.

Before taking a closer look at risk types in life assurance and their methods of management, let us attempt to define what we mean by the term risk management. Dorfman (1994) defines risk management as a long-term process utilised by individuals and companies for the management of exposure to potential loss. Therefore, risk management is a continuous process in companies, aimed at realising the minimum loss and maximum benefit possible (Turk 2002). In general, the risk management process in a company can be broken down into three steps (Harrington 2003):

Slovenia's life assurance market is still rather traditional despite a host of recent changes.

1. identification of all of the more important risk types in a company
2. risk modelling, monitoring and measuring
3. introduction of a risk management system.

Here, the notion of risk must be understood especially in its financial and legal meaning, and should not be equated with the insurance term of risk or peril which marks the contents of insurance (Pavliha 2000). The notion of risk must be dealt with in a broader context, as it contains both elements which can be the subject of insurance and those which are not. For instance, risks which companies are exposed to due to the external economic environment or the legal framework are only rarely the subject of insurance in classical terms. However, a modern company must also be able to identify, measure and manage those risk types that cannot be managed through insurance in the classical sense of the word.

RISK MANAGEMENT IN LIFE ASSURANCE

When talking of risk management in life assurance, we must first define the risk categories to which insurance companies operating in the field of life assurance are exposed. Porlan (2002) defines the following sources of risk in life assurance:

1. Interest rate risk
2. Credit risk
3. Insurance risk
4. Cost risk
5. Operational risk
6. General business risk.

As emphasised in the introduction, risk management in a company can be viewed as a continuous cyclic process which is divided into three levels. At the first level we speak of the identification of possible risk types, i.e., of the definition of individual factors that increase the risks in a company. Here we can use Porlan's classification of possible risk types in life assurance, although we must take into consideration the fact that insurance companies dealing with life assurance are exposed to the individual risk categories in different ways. Thus, for a small insurance company, cost risk may be a much larger threat to successful operation than to a large insurance company with a strong capital background and more able to utilise synergy effects and the economies of scale.

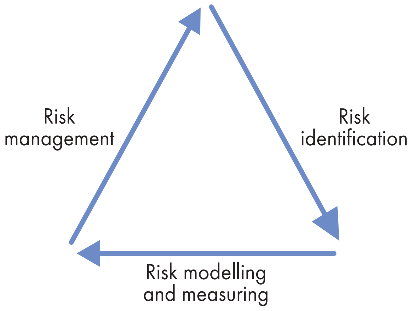
At the second level, individual risk types are modelled and measured. Thus, models are obtained on the basis of which the level of exposure of the insurance company is established for an individual risk segment. An example of this is interest rate risk, which has lately been very topical for insurance companies. The probability model helps us to establish the extent to which the movement of interest rates can affect the long-term fulfilment of obligations. The exposure of the insurance company to interest rate risk is, to a large extent, dependant on the nature of the insurance products it offers. From the point of view of the insurance company, insurance with a guaranteed rate of return poses a much greater risk than other forms of life assurance. An insurance company offering only those forms of insurance where the policy-holders take over the investment risk in this segment in full is, of course, not exposed to interest rate risk.

The modelling of various scenarios of interest rates helps us to determine how they affect the expected financial and other accounting indicators, as well as other indicators, in a company. Monte Carlo interest rate simulations can help us to establish the exposure of an insurance company to interest rate risk for each scenario. Each trajectory represented by one of the possible scenarios of future interest rate movements is obtained on the basis of an assumed distribution. We obtain the result of the total exposure of an insurance company to interest rate risk by taking into account the probability distribution of individual scenarios.

Based on the identification and measurement of risk in an insurance company, management can take appropriate measures for its alleviation or control (level three). Leverages available to management are diverse, and depend mainly on the level of exposure and the risk type. Depending on the risk type, these can include measures concerning investment policy, development of new products, the claims settlement process, the process of acceptance into insurance, reinsurance and similar.

Regardless of the measures taken by an insurance company in order to manage risks, it must have appropriate capital readily available at all times. This capital enables it to constantly fulfil all of its obligations according to the scope and type of insurance it offers. In line with the Insurance Act, Article 104, the insurance company must operate in such a way that the risks it is exposed to in insurance operations never exceed the limits set by this Act. Therefore, an insurance company must constantly follow capital requirements, the insurance

Figure 1: Risk management process is made up of three levels



and technical provisions, the values of the long-term business guarantee fund, types, dispersion, harmonisation, localisation of investments of cover assets, etc. The existing rules and regulations on the calculation of capital adequacy ratio are, however, fairly rigid, as they do not take into account the level of the insurance company's exposure to individual risk types. The calculation of the amount of minimum capital is thus based on a simple mathematical formula which does not, for instance, take into account the level of insurance company exposure to investment risks. More recent methods for calculating minimum capital, such as risk-based capital (RBC), better take into account the nature of the individual risks an insurance company is exposed to. With the introduction of new international accounting standards, such methods will become standard in Slovenia, too.

To conclude this section, let us try to make a graphic illustration of a risk management process in an insurance company. Figure 1 shows that the risk management process as a continuous cyclic process is made up of three levels. An insurance company wishing to set up an efficient risk management system must provide the organisational and staff-related conditions for the implementation of all three phases within its organisation. Because of this, some insurance companies abroad have already established separate organisational units specialising in comprehensive risk management in the company.

In the continuation we will take a closer look at those risk types to which insurance companies dealing with life assurance are most exposed.

Interest Rate Risk

Recently, one of the major challenges of insurance companies, especially in the field of life assurance, has certainly been interest rate risk management. Due to falling interest rates, the interest rate income of insurance companies is decreasing, which lowers the expected profit participation in life assurance profit and further threatens the solvency of insurance companies. A special feature of life assurance is that a guaranteed interest rate (the so-called technical interest rate) is set in advance for the whole insurance period, and cannot be changed in the duration of an insurance contract without the prior consent of the policy-holders. As life assurance contracts are usually long-term contracts, with a 10-year maturity or more, insurance companies are, in the case of life assurance with a guaranteed interest rate, generally exposed to the risk of being unable to fulfil long-term obligations related to interest rates. Exposure levels depend on the level of the guaranteed interest rate and the type of guarantee which an insurance company underwrites with the insurance contract.

Generally speaking, the main characteristics of interest rate risk occurring in life assurance can be broken down into the risks related to reinvesting investments falling due, risks related to investing future premiums from existing contracts, and risks related to unbalanced investments and obligations, especially with regard to maturity, nature, and currency. The risk related to reinvesting investments and unbalanced investments and obligations could be placed in the same category as they pose a similar problem for insurance companies: how to find, in the changed conditions of financial market operation, an appropriate substitute investment to cover the obligations ensuing from insurance contracts signed in the past. Risks related to investing future premiums occur because it is impossible to predict in advance whether an insurance company will be able to invest a current premium under similar conditions for the whole period of life assurance duration.

A special problem in interest rate risk is represented by the manner of evaluating assets and liabilities. In life assurance, insurance companies have to design mathematical reserves in the amount of the expected current value of future liabilities, less the expected current value of future paid premiums. Mathematical reserves are an integral part of the mandatory cover which also includes loss reserves and transferable premiums reserves. According to the Insurance Act, an insurance company must guarantee that the cover fund, which by definition is an asset intended for fulfilling the obligations arising from life assurance, is at least the same as the required cover at all times. Therefore, in the first place, it is important that the manner of evaluating assets and liabilities are harmonised. In the market evaluation of the long-term business fund, however, this is possible only if the liabilities are evaluated in accordance with their fair value (the so-called fair value approach to liabilities evaluation), which the currently valid accounting standards do not enable. Mathematical provisions are calculated with a mathematical formula, hence the name, which in addition to a probability component also takes into consideration the level of the guaranteed interest rate. Fair value, or market value, of liabilities is established by taking into account the average market value of zero-coupon bonds with the same maturity as liabilities assumed under insurance contracts.

The basic measure available to the insurance company in interest rate risk management is certainly an appropriate investment policy which helps the insurance company to harmonise obligation maturity with investment maturity, thus decreasing the problem of imbalance. Here, insurance companies make use of various ALM models (assets and liabilities modelling) for monitoring and controlling the exposure ensuing from an imbalance between investments and obligations.

When the income from cover fund investment no longer suffices to cover the guaranteed interest rate, or when it is anticipated that there is a certain probability that the investment returns in the future will not suffice to cover liabilities from interest rates, the insurance company has to design additional provisions over and above mathematical provisions for interest rate fluctuations. The shaping of additional provisions along with the mathematical provisions is a measure also provided for by the EU Directive on life assurance. In accordance with this directive, the insurance company may form additional provisions within mathematical provisions for those risks that cannot be defined on the level of individual insurance, but can be assessed on the level of the whole portfolio. Of course, in order to decrease interest rate risk, it is easiest for management to take appropriate measures in the development phase of new products. The parameters determining the amount of the insurance premium should be thoroughly analysed and set in a scope that, by taking into consideration prudence and safety, guarantees the long-term fulfilment of its obligations.

Risks associated with costs occur when spending gets away from management control.

In terms of life assurance, the Slovene insurance market is still rather traditional, although we have witnessed numerous changes in this field in recent years. The major share of life assurance in Slovenia is represented by classical insurance products, such as combined life assurance, where an insurance company guarantees an interest rate set in advance. The interest rate is now limited to 3.25% per annum to the amount of mathematical provision. In view of the falling trend of interest rates, we can expect a further decrease in the technical interest rate to below 3% per annum. Here, we have to stress that an insurance company in classical life assurance, such as combined life assurance, guarantees a technical interest rate to the amount of mathematical provision and not to the paid-in premium – mathematical provisions are only filled from that part of the insurance premium intended for the savings component of the insurance contract.

Prior to Slovenia's entry to the EU, insurance companies operating in the Slovene insurance market were subject to fairly strict and restrictive legislation, which also applied to the investment policy. Thus, special approval of the regulator was required for investments in the EU. Because there were not enough appropriate investments in Slovenia with fixed returns and maturities corresponding to long-term liabilities (e.g. bonds falling due in 20 to 30 years), insurance companies invested the majority of their funds from mathematical provisions in deposits and the available state securities. With Slovenia's joining the EU, insurance companies certainly have enough investment instruments to decrease interest rate risks. However, due to the adaptation to, and study of, new investment opportunities in the EU, the process of harmonising investments and liabilities will be a gradual one, especially in terms of investment maturity.

Since 2002, insurance companies operating in the Slovene market have started to actively market insurance where the policy-holders underwrite investment risk. The current trends show that such insurance will prevail in the future. This will also decrease the importance of the interest rate problem, as in the majority of cases it does not exist in investment insurance – investment insurance being a form of life assurance where the insurance company transfers the investment risk to the policy-holder.

Credit Risk

When speaking of credit risk, we usually refer to the so-called default risk in investment in bonds and the default risk in reinsurance companies. Credit risk in relation to reinsurance companies is a special feature of insurance companies and represents an important category of risk, especially in insurance companies dealing with life assurance. The insurance company must reinsure those shares of insurance cover which exceed its own shares, as defined in the maximum cover tables. With reinsurance, the insurance company transfers part of its own insurance risk to another legal entity in return for the payment of an appropriate reinsurance premium. If at a certain point in time the reinsurance company is no longer able to fulfil its obligations to an insurance company arising from covering the reinsurance part of loss, this can place the direct insurance company, in the event of a major loss claim, in a difficult position in terms of liquidity and solvency. Therefore, it is of the utmost importance for insurance companies to continuously follow the credit evaluations of reinsurance companies with which they work.

Insurance Risk

Risks related to underwritten risks are a special characteristic of insurance companies, given that in the case of signing an insurance contract between the insurance company and the insured the risk for the occurrence of the event determined in advance is transferred from the insured to the insurance company. As management of risks arising from insurance risks is the basic activity of every insurance company, this is the area to which insurance companies devote most of their attention. This group of risks also includes the forms of risk arising from insurance-related business processes. The basic business processes related to the life assurance operation thus comprise:

– development of new products
– sales and marketing of insurance products
– acceptance into insurance
– settling loss claims
– reinsurance
– investment operation
– administering insurance

As the problem related to investment operation has already been dealt with separately, we should now take a closer look at the risks related to acceptance into insurance, reinsurance-related risks and risks related to the development of new insurance products.

Risks related to acceptance into insurance are most linked to the problem of asymmetrical information. When the insurance company is estimating the risk it will be exposed to upon signing an insurance contract, it needs appropriate information on the insurance subject. If the insurance company has enough information available on the medical condition of the insured, it can accurately asses the scope of the underwritten risk and define it as such in the amount of the insurance premium. In practice, however, it is impossible to acquire from all insured persons data of sufficient quality to make an accurate assessment of the amount of underwritten risk. Therefore, there is a risk that the insurance company will accept into insurance higher risks than assumed when developing an insurance product, which means that it will not calculate an appropriate insurance premium for the underwritten risk.

Reinsurance-related risks are risks of a non-credit nature, and are a result of the management decision on the reinsurance type. When an insurance company is introducing a new product, or when it is introducing a risk with which it has no empirical experience, suitable reinsurance is of paramount importance for appropriate risk dispersion. Furthermore, reinsurance can also be an instrument of capital adequacy equalisation, especially with small insurance companies.

In the development phase of a new insurance product it is very important to be able to adequately assess the parameters which define the insurance premium. The risk which the insurance company underwrites upon signing an insurance contract is reflected in the insurance premium in terms of price. An insurance premium is thus an insurance company service expressed in price and defined in the insurance contract between the policy-holder, the insured person and the insurance company. An insurance premium in life assurance in general depends on:

1. likelihood of a loss event
2. interest rates
3. insurance sum, and
4. costs incurred.

An incorrect estimate of individual parameters determining an insurance premium in the phase of new product development represents a risk for the insurance company to which it is exposed during the whole life cycle of the insurance product.

Cost Risk

As found by Porlan (2002), until now, cost risk has been dealt with as part of operational risk. However, due to the increasing importance of cost management in insurance companies, today both theorists and experts from practice define cost risk as a separate category. With decreasing profit from the insurance-technical result of life assurance, and decreasing returns from interest rates, management boards of insurance companies are forced to focus more and more on cost risk management.

The cost-related risk factors in life assurance can be:

– inappropriate cost calculation
– high costs of insurance acquisition, and
– uncontrolled increases in costs.

Appropriate calculation of costs is related to the quality of the cost accounting system. In the event that the cost accounting system in an insurance company does not provide an appropriate distribution of general costs by cost bearers and cost centres, the management board does not have appropriate information on its own pricing of insurance products. So the management board can have incorrect information on product, client or distribution channel profitability, which can lead to incorrect business moves. An appropriate dispersion of costs to cost centres and cost bearers is, therefore, the basis for successful cost risk management. Methods that distribute general costs on the basis of business process activities, such as the ABC method (activity based costing), yield better results of cost accounting and thus provide a more realistic picture of one's own pricing of insurance products. Furthermore, cost monitoring by business process activities helps us to acquire much more information on the cost effectiveness of processes and activities, which the management board can then turn to their advantage in terms of cost risk management.

Insurance acquisition costs are an important segment of operational costs in life assurance, as they usually represent more than a half of the insurance company's total costs. In order to understand why this is so, let us look in detail at the operational cost structure in the insurance company. In the insurance product life cycle there are three periods with regard to costs. The first period comprises the time of taking out an insurance contract with which the insurance acquisition costs are related. Insurance acquisition costs do not only comprise the costs of commissions paid to the sales network, but include all costs related to the taking out of a new insurance policy, i.e., promotional and other costs. Therefore, these costs are by far the greatest in the whole product life cycle. The second period comprises the time of active insurance management lasting until the termination of the insurance relationship and/or until the preceding insurance event. The third period comprises the time when an insurance event occurs and to which appraisal costs are related. A special characteristic of costs in connection with life assurance is that they occur irregularly during the insurance period. High start-up costs (insurance acquisition costs) are followed, in the time of insurance duration, by proportionally lower renewal costs and somewhat higher appraisal costs. As insurance acquisition costs represent the main body of the operational costs of the insurance company, it is precisely these costs that are exposed to the risk of rapid growth. Risks related to the high cost of insurance acquisitions occur mainly in the case of rapid growth of the insurance company in terms of acquiring new insurance contracts, when their number increases to such an extent that the insurance company is no longer capable of covering them.

We speak of the risk related to the non-management of costs mainly when costs "get out of the control" of the management board, or when the actual costs substantially exceed the calculated costs which are factored into the insurance premium. Methods such as Activity Based Management (ABM) and Target Costing (TC) or other established methods of cost management can help management to successfully control increasing costs in the insurance company.

Operational Risk

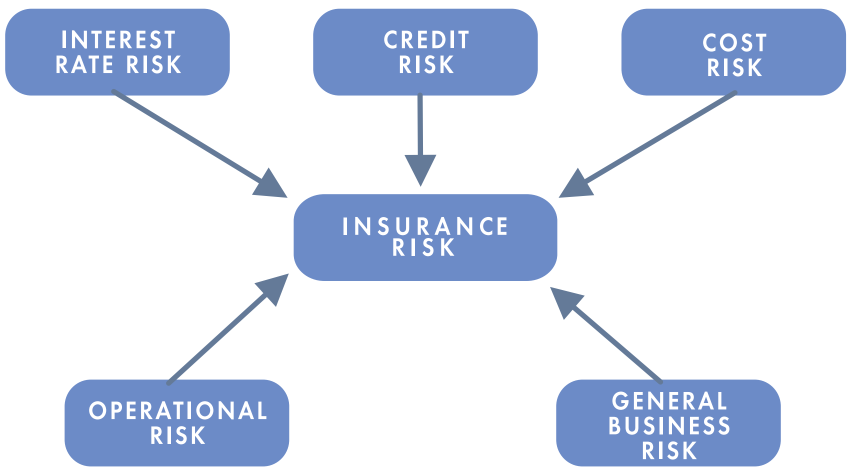
The changes in technologies that we are witnessing today will certainly lead to changes in financial services market operation. Today, the internet has changed our perception of financial services in many ways. Modern technologies enable companies to have more and more information about their customers available. This also enables them to upgrade their strategies with cross-selling, while also enabling the segmentation of customers by profitability and other indicators. Last but not least, modern technology enables greater automation of the operation which, in the long-run, can decrease operational costs. In developed economies, systems such as "point of sale underwriting" and the like have already gained ground, as they represent a decrease in administration costs for the company, and faster contract processing for the customer. However, new technologies also bring about new forms of risk. A good example of how modern technology, in itself, is not enough is the Sigma project, which the bank Nova Ljubljanska banka d.d. tried to introduce, but failed mainly due to strategic mistakes in project management.

Among operational risks in insurance are mainly risks related to mistakes in the operation of business processes, information technology, organisation, etc. In this part, operational risks do not differ greatly from operational risks in other financial institutions, so we will not go into detail on this topic.

Table 1 which follows presents a short overview of risk categories related to life assurance activity complete with possible measures for risk measurement and management.

Risk category	Risk models and risk measurement	Management option
1. Interest rate risk	ALM, Monte Carlo	ALM, product adjustment, Earmarking additional reserves
2. Credit risk	Credit assessment	Investment policy
3. Insurance risk	Actuaries control cycle	Changes in insurance products
4. Cost risk	ABC	ABM, deferred insurance acquisition costs, TC
5. Operational risk	Measuring and monitoring of business processes	Balanced scorecard (BSC)
6. General business risk		Legislation monitoring

Figure 2: Insurance risk management



General Business Risk

General business risk is related to the operation of the insurance company in the environment and space, such as the economic environment, legislation and similar, and which the insurance company often cannot directly influence. Therefore, such risks are difficult to measure and/or model. Nevertheless, we should mention here the risks related to the changed circumstances which Slovene insurance companies will have to face now that Slovenia has become a full member of the EU.

Both life assurance directives and the new insurance legislation introduce a system of the uniform issue of authorisations for undertaking insurance activity, as well as a system of uniform control over the operations of insurance companies. This means that every insurance company can operate in any EU member state based on authorisation issued by an authorised supervisory body in the home country. The development of directives will surely go in the direction of further liberalisation of operation, mainly in the sense of uniform taxation of insurance and enforcement of new international accounting standards. In the future, the introduction of fair value in the evaluation of liabilities, ALM, RBC and similar instruments of risk management will have a major impact on the current risk management processes in insurance. By joining the EU, Slovenia has become part of the single European insurance market with all its advantages and weaknesses. Insurance companies which are not well prepared for the changes we are witnessing today, and which do not intend to also seek new opportunities outside the Slovene borders, will become easy prey for acquisitions by other companies.

CONCLUSION

Companies wanting to survive in the changed business environment will have to pay greater attention to risk management. Insurance companies are no exception to the rule. As well as managing other types of risks that are present in every company, insurance companies also have to manage insurance risk, i.e., risks transferred to them by their clients, the insured. Insurance risk management is in the focus of every insurance company together with interest rate risk, general business risk, credit risk, operational risk and price risk, as shown in Figure 2. Only an insurance company able to appropriately identify, measure and control the aforementioned risks, and, last but not least, manage them, will be a successful insurance company.

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Supplementary Pension Insurance in Slovenia

*Helena Bešter**

SUPPLEMENTARY PENSION INSURANCE IN SLOVENIA
Supplementary pension insurance which was introduced in Slovenia four years ago has been successfully developing. The stabilization of the markets providers is coming to an end since the market shares are divided among six the biggest players although it is expected that their number will be reduced due to more cost efficiency. Within the frame of the further development some of the main issues will have to be solved; the issues which have a significant impact on the quality of additional pension products as well as on the financial strength and the stability of the providers. The same rules for all the types of the providers will have to be set up, and therefore the direct comparison of their performances will be able to be measured. The minimum return guarantee will have to be changed in such a way not to threat the financial stability of the providers, and to adapt to the long-term characteristics of the pension insurance. Because of all the mentioned issues and because of the implementation of the IORP Directive, the provisions of the Pension and Invalidity Law will have to be changed significantly. Also the subject of the annuities will have to be settled as soon as possible.

Due to rising longevity, the period of time an individual spends »in retirement« has become longer. If just over a hundred years ago people lived as pensioners for some years only, today those who after completing their active working lives go on for not only a couple of decades, but thirty or forty years are much more common. This means that they receive pension benefits for a period being almost as long as the period of their employment.

The article describes the general causes as to why the role of supplementary pension insurance (occupational retirement provision) is becoming ever more important. The volume of assets being paid into institutions for occupational retirement provision – pension providers – has also been rising accordingly. To draw comparison, the article moves on to the key parameters which determine the long-term balance of the state pension system in Slovenia and the European Union. Slovenia's pension system displays through most of its features that despite the reforms accomplished, it is in worse shape than the EU is on average. A description of different kinds of pension providers follows complete with an outline of the development of the Slovenian market for supplementary pension insurance as witnessed so far. Slovenia has designed some rather innovative solutions in this area, which have practically no comparison elsewhere.

A layout of the characteristics of the Slovenian pension system and comparison with the EU

The landmark feature of the Slovenian pension reform, implemented by adopting a new pension law which entered into effect

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in 2000, is its gradual approach. The contraction of rights has been slow and will continue until the year 2017. The level of employee contributions has long been insufficient to cover pension costs under thesocial security, i.e. state pension system. The figures budgeted for 2004 show that 30.84 per cent of assets required for state pensions will be covered from the so-called income transfers, of which direct appropriations from the budget meet 29.42 per cent of all foreseen expenditures. Pension expenditure accounts for 13.78 per cent of GDP, with the ratio between pensioners (beneficiaries) and insured persons (members) shrinking in 2003 to a meagre 1:1.57 (Monthly Statistical Overview, 2004).

Despite the high expenses incurred under the state pension system, it is clearly visible that the ratio between salary and pension benefits has tumbled. If in 1992 the average pension benefit accounted for a hefty 77.8 per cent of the average salary, in 2003 it was only a mere 71.1 per cent of the average salary. If the downward trend were to continue at unchanged intensity, over, let's say, the next 20 years, it would mean that pension benefits in 2030 would account for less than 60 per cent of salary. Are we to expect that in ten or twenty years' time the standard of life enjoyed by present employees at the time of retirement, would be halved unless they made arrangements for supplementary retirement provision? Such expectations are totally realistic. The bottom line is that the data benchmarking the Slovenian state pension system against the EU social security schemes are not very good.

The share of expenditure allocated in the EU for the payment of pension benefits from state pension systems, accounted for 10.4 per cent of GDP in 2000. Nevertheless, the disparities between EU Member States are huge both in terms of organisation and principal indicators used to define the long-term stability of social security systems. While pension expenditure in Great Britain amounts to only 5.5 per cent of GDP, Italy seems as generous as Slovenia (13.8 per cent), while Austria has record expenditure of 14.5 per cent of GDP. Even a quick screening of EU Member States clearly shows that pension expenditure below 10 per cent has been achieved, as a rule, in those countries where supplementary pension provision is developed. Forecasts made until the year 2040 are vastly different as well. The average level of the EU portion of pension expenditure as a per cent of GDP has been set at 13.6 per cent, hence slightly less than we are even now spending in Slovenia, of which the pension expenditure share will drop in other countries (e.g. Great Britain) below 5 per cent, and in other countries such as Greece for example, it is due to even exceed 20 per cent of GDP (The Council of the EU, 2003)[1] . Such steep growth in expenditure is associated with the demographic forecast: lifespan is increasing, new births are sparse, and Europe is indeed becoming an aging continent as we speak. If in 1960 the so-called dependency ratio[2] stood at 16 per cent, in 2000 it soared to 24 per cent. According to the projections made by Eurostat which compute this indicator as the ratio between the population 65 years of age and over and the population between 20 and 64 years of age, the share of senior citizens will rise to 53 per cent in 2050 (Social Protection Committee, 2001). In plain language, those who will have to foot the pension bill will be outnumbered by the beneficiaries.

Given the forecasts it is clear that pension benefits provided under state pension systems will have to be trimmed further. This applies to Slovenia and all other European countries that are still paying their beneficiaries relatively high pension benefits in comparison to salary. The present medium-aged and younger population will live to see many a pension reform. In the aftermath of each of these, the government will cut entitlements arising from the state pension system and give more weight to supplementary pension insurance. In other words this means that government will be shifting the burden of making provisions for appropriate pension income to individuals. As we move on, let's see how supplementary pension insurance has developed in Slovenia so far.

Development of the supplementary pension insurance market

Gradual but persistent withdrawal of the state from the pension provision system cements the conviction that supplementary retirement provision is indeed a must. The conditions for putting in place a new pensions framework in Slovenia were created with the most recent pension law which came into effect on 1 January 2000 and has been modified and amended several times since then (ZPIZ, 2004).

The law stipulates that the range of institutions for supplementary (occupational) retirement provision (the providers) includes: life assurance undertakings, pension companies and mutual pension funds. The prerequisite for taking up the business is an approved pension scheme. The green light for pursuing this line of business is "lit" by the Minister for Labour. Having met this requirement, life assurance undertakings qualify to enter the market. As for pension companies, in addition to the approved pension scheme, authorisation to take up and perform this business has to be granted by the Insurance Supervisory Agency. The Securities Market Agency authorisation for establishment is mandatory for mutual funds.

In the Act, the law-maker has envisaged that mutual pension funds and life assurance undertakings are the main providers of supplementary pension insurance. Consequently, the provisions of the Act referring to the operations of pension companies remain silent on many issues and often direct us to the Insurance Act. All more significant provisions, which determine the principal insurance characteristics (keeping personal accounts, investment risk, calculation of profitability and costs) have been written for mutual pension funds. It was not before the modifications to the Act were

[1] If Slovenia had failed to embark on pension reform, the portion of expenditure for pension payouts made under the state pension system would have hit 26 per cent in 2040.

[2] The traditional »dependency ratio« is calculated by dividing the portion of population aged above 65 by the number of individuals aged 15 to 64 expressed as percentage.

adopted that these provisions also apply *mutatis mutandis* to pension companies and insurance undertakings. Originally, the Act laid grounds for employers to set up close-ended mutual pension funds for the provision of supplementary pension insurance as in-house funds or industry-wide funds.

Life eventually took its own, different course. Instead of mutual pension funds, enterprises decided to establish, together with other enterprises, pension companies as a special, specialised form of insurance undertakings. The provision of supplementary pension insurance in addition to the cost of premiums also meant the cost of capital that pension undertakings require for their operations. Enterprises have included pension companies as specialised financial institutions among their connected companies, and so entered the insurance services market "through the back door". Insurance undertakings have also taken a similar irrational decision, even though under the Pension Act they enjoyed a privileged status and had the easiest entry into the market. While prior authorisation granted by the supervisory authority is mandatory for establishing a pension company or a mutual pension fund, the way was paved for insurance undertakings to enter the market directly and immediately after approving the pension scheme. This advantage of providing a straightforward approach was of key importance at the beginning and meant a huge time advantage and was fully exploited only by Triglav insurance company. All other insurance undertakings have missed out on this exceptional business opportunity. Instead, together with banks they followed in the footsteps of larger companies and started to establish pension companies – a real hit in the year 2000. On top of that, the banks as significant co-founders of certain pension companies, were keen to cut their slice of the pension cake too by setting up their open-ended mutual pension funds. The euphoria of establishing institutions for the provision of supplementary pension insurance has led to an overcrowded market, fierce struggles for market share, and in the case of pension companies also an exploitation of the loopholes created by imperfect Pension Act legal provisions. Ne spreminjati tega stavka, ker lektor ni razumel bistva.

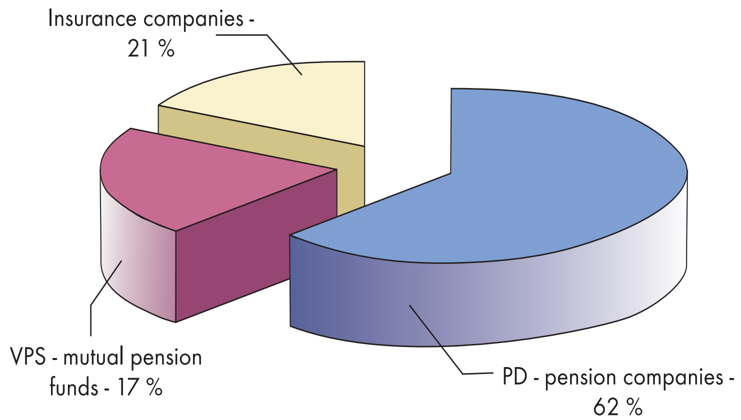
In 2001, just over a year after the Pension Act entered into effect, there were four pension companies competing for market share, plus six mutual pension funds and three insurance undertakings – the total of 15 providers. Even laymen could see that not all of them would survive. When fighting for members, pension companies did not have a level playfield since they had to arrive at 15,000 members after two years of operations. The regulatory threshold for mutual pension funds was set at 1,000 members, while no quantity limit was set as binding upon insurance undertakings.

Even though during the first years when start-up costs are at peak values, cutting back product prices is not economically justified, the tug-of-war raging among the providers of pension insurance for members has forced them to reduce entry and exit commissions, and management charges below any reasonable limit. The providers waging a cost war that broke out on that occasion were counting on being able to achieve sufficient economies of scale by means of dumping prices in order to stay afloat even at extremely low prices of insurance. Most of them were wrong in their calculations: in the light of the present distribution of the market, the scale of operations is too modest for more than one provider to enable long-term survival. The exceptions are the providers holding the largest market shares provided that they have quality portfolio members – regular contributers with high average premiums.

In the race against competitors, two pension companies, one mutual pension fund and one insurance enterprise have already given up. Their portfolios of insured persons (members) have been transferred to other pension providers. Eleven institutions out of the pack have stayed on track: among five mutual pension funds, there is only one larger, out of two insurance undertakings there is also just one large, four pension companies remain on the battlefield. Two pension companies are contemplating transforming into a life assurance company. As a result and due to plans for creating strategic alliances, and maybe even performing take-overs, we may expect the number of pension companies to be reduced in the future[3].

The number of pension scheme members was rising vigorously from the beginning of 2001 until the end of 2002, and as of the last day of 2003 totalled 210,463. In an effort to attract members, pension companies outperformed their rivals: as much as 62 per cent, i.e. 130,702

Figure No. 1: Composition of the supplementary pension insurance market by members as at 31 December 2003



Source: Ministry of Labour, Family and Social Affairs

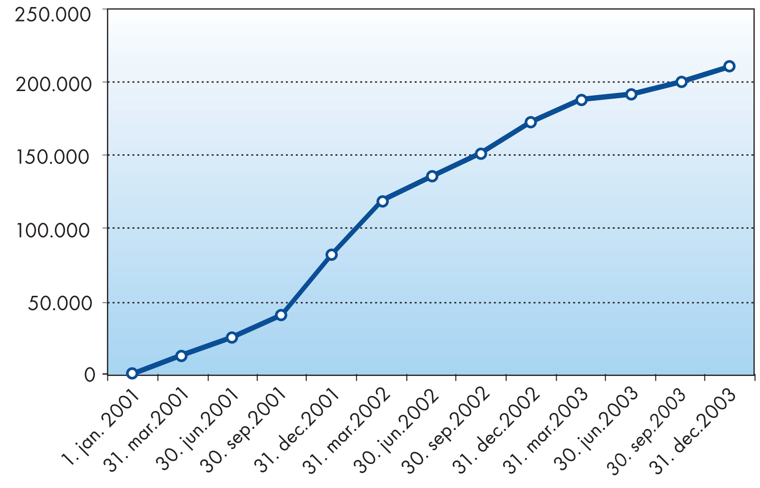
[3] Pension companies are a Slovenian speciality. The current trend in the development of the market and the industry (aspirations to transform to insurance undertakings) indicates that in spite of the high number of members, this type of provider is in a sort of crisis, and it also suggests that being innovative at any price does not necessarily mean higher quality.

members joined their schemes. Insurance undertakings attracted 43,188 members, i.e. 21 per cent of the overall number, followed by the mutual funds which lured 36,573 members or 17 per cent of the overall number.

According to the available data, there are just over 10 per cent of members in individual (personal) pension schemes, the majority are covered by collective (occupational) pension schemes. Most »individuals« are insured at Triglav insurance company.

The picture changes when we examine the distribution of market shares in terms of asset value; in particular, the aggregate market share of pension companies and insurance undertakings in terms of the number of members is 83 per cent, while in terms of the volume of assets it is 75 per cent. Mutual pension funds have a 25 per cent of market share, of which the share of the largest pension fund in terms of asset value stands at 77.59 per cent. The largest provider among pension companies and insurance undertakings has a 30.71 per cent market share in terms of asset value (Bulletin *Financial Market in Slovenia*, 23/2004).

Figure No. 2: Growth in the number of members covered by voluntary supplementary pension schemes by quarters from 1 January 2001 to 31 December 2003.



Source: Ministry of Labour, Family and Social Affairs

Underwriting supplementary pension insurance was highly intensive in 2001 and 2002, when the number of pension scheme members climbed in two years' time to 173,044, which means 81.49 per cent of all members as at 31 December 2003. In 2003, growth slowed down and in 2004 almost came to a standstill. According to the pension providers, at mid-April this year the number of members totalled 212,355[4] (Petrov, 2004). This means that since the end of 2003 this number has increased by a mere 1,892 members, i.e. by 0.90 per cent. On the one hand, the pension market was already divided (most large and successful companies had already signed up), and on the other hand, the pension providers were waiting for the last, the biggest and sweetest bite – retirement provisions for public sector employees.

By including public servants, which happened in April this year, the number of members increased by 154,396. The total number of members rose to 366,751, which means 45.38 per cent of all people included in the state (compulsory) pension insurance. With such a share of employed persons included in voluntary supplementary pension schemes, Slovenia is firmly on track to join the ranks of the countries where pension system with the so-called second pillar of occupational schemes is in place. It serves as a framework for the bulk of employees to ensure a flow of income for retirement through the employer.

Challenges brought along by supplementary pension insurance

Even though the quantitative data on the development of supplementary pension insurance over the last three years may appear rather promising, this industry is faced with numerous challenges, which call for fast and effective solutions. If we have been paying attention so far to quantity, the quality of insurance has to take the centre stage role, particularly in the overhaul of regulations, adequate solutions as to guaranteed return, and by implementing the so-called pension or IORP directive - Directive on the activities and supervision of institutions for occupational retirement provision.

The provisions laid down in the Pension and Disability Insurance Act should be thoroughly re-examined, and the rules governing operations of institutions for supplementary (occupational) pension provision should be unified. It is worth exploring the possibility of drafting a special law to govern supplementary pension insurance and preserve the connection with compulsory pension insurance only where necessary and up to the level necessary to ensure the integrity of the pension system. The next step will be the harmonisation and unification of secondary legislation, since under the current regulatory arrangements, pension products of different kinds of institutions for supplementary (occupational) retirement provision cannot be compared at all. More security and less room to manipulate members and beneficiaries would eventually mean unification of prudential supervision and standardisation of the rules governing dissemination of information to members.

As far as guaranteed return is concerned, it is time to reconsider whether we need this instrument at all and evaluate how much it really contributes to increased security for members and their assets. Furthermore, monthly benchmarking of the rate of (un)successfulness of investments which deploy long-term savings as pension benefits, makes little sense. When determining the rate of return to be generated by investments of pension assets, the Pension Directive makes reference to a maximum allowed interest rate: »When setting the maximum interest rate,

[4] Members who pay premiums have been taken into account.

[5] Directive 2003/41/EC of the European Parliament and of the Council of 3 June 2003 on the activities and supervision of institutions for occupational retirement provision.

the return currently available and the expected future return on assets, and the return on government or high quality bonds, as arising from prices on the securities market, should be taken into account« (Bešter, 2004).

In addition, the IORP Directive[5] brings in a number of provisions governing the activities and supervision of institutions operating occupational pension schemes, and Slovenia has a lot to do in this area, particularly in the area of regulatory own funds, drawing up financial statements and reports for supervisory authorities, and notifying members. There will be fewer difficulties when transposing investment regulations, since the Pension Act already contains many provisions cross-referenced to the Insurance Act. The Directive lifts barriers to cross-border activities both to the providers of pension schemes and the managers and custodians or depositaries of their assets.

On top of all that has been said so far, there is yet another challenge in store for us: adequate regulation of supplementary pensions, i.e. annuities. The effective regulations govern only the period of savings, while the length of the period during which payouts will be made is a completely grey area and an unknown factor.

Conclusion

Slovenia has been making long strides in the area of supplementary pension insurance and over the four-year period after the promulgation of the legislative framework has included just under half of the employed population through insurance. This ranks Slovenia, in terms of the number of members, among the countries regarded as more advanced in this respect. On the other hand, Slovenia is struggling to get over a number of teething problems such as a price war, an unyieldingly high number of pension providers, discordant legislation, incomparable pension products, incomplete information provided to members, and often shallow professional knowledge.   V drugem stavku sklepa naj ostane "persons in employment", oz. popravek ni potreben.

Due to the high number of pensioners and the large slice of GDP even currently allocated to pensions under the compulsory state system, the level of these pensions in the future is bound to dwindle. Supplementary pension insurance will have to fill the gap in retirement income. Consequently, it is of paramount importance that this industry in Slovenia has a firm foothold and stabilises. In addition, an adequate legislative framework coupled with prudential supervision has to be put in place so as to ensure smooth and successful implementation of pension schemes. It is the only way in which, after retirement, the present members can improve their position as beneficiaries through supplementary pension benefits.

Supplementary pension schemes in Slovenia are new entrants in the market. It is the most plausible reason why they are faced with a host of concerns and problems, and a solution to these problems has to be worked out as a matter of priority. Any postponement of adequate solutions may lead to a crisis and major problems eventually resulting in negative consequences on further development in this area. For Slovenia it is equally important to start transposing the occupational pension insurance rules laid down in the EU Pension (IORP) Directive as soon as possible. Although there is over a year to deal with it, it would not be wise to delay prompt implementation of the Directive on the activities of institutions for occupational retirement provision and also appropriately adjust supervision of their operations. How successful we are at doing this will determine the further development of supplementary pension insurance and it will eventually determine whether in this area Slovenia will become/remain a sovereign player or it will helplessly watch how its pension savings are managed and administered by others.

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"Kasko" Motor Insurance – Austria, Italy, Slovenia

*Edi Glavič**

"KASKO" MOTOR INSURANCE – AUSTRIA, ITALY, SLOVENIA
The insurance market for KASKO insurance is similarly organised and developed in all three countries compared. There is more choice of insurance coverage in Austria and Slovenia than in Italy, and the participation of the insured is lower as well. Unlike in Austria and Italy, in Slovenia negative claims ratio trends can be observed in the last few years. With respect to the coverage of the insurance market, a large number of insurance companies offering KASKO insurance, strong competition and negative claims ratio, it is not to be expected that a large number of new insurance companies will be interested in the Slovenian KASKO insurance market. It is possible that the KASKO insurance coverage will be offered by new insurance companies mostly to their clients as a part of a complete offer of insurance.

A comparison of the insurance markets of the three neighbouring countries is of special interest because of the fact that Austria and Italy have been in the EU for years while Slovenia just entered this union.

Generally the term "KASKO" in all three countries means insurance coverage covering damage caused to the insured vehicle by the driver or other external factors. As will be seen further on, differences are present as well. In countries subscribing to the Anglo-Saxon model of insurance, the term "comprehensive insurance" is in use for "KASKO".

GENERAL FINDINGS

In the three countries, quite a few insurance companies offering the insurance product mentioned have been present on the insurance market for a number of years.

In Austria insurance conditions had been approved by a national supervisory body until 1994, products were similar to each other, there were only small differences in price. In 1995, Austria enters EU and a full-scale deregulation takes place[1].

In Italy insurance conditions and the rates of insurance premiums have been in the exclusive domain of insurance companies for a longer period of time. The scope of insurance coverage, participation of the insured, and prices have thus been determined by the market.

Slovenia can be observed as an independent country since 1991, when five insurance companies offering KASKO insurance

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[1] The data for Austria were presented at 10th seminar Motor Insurance, Maribor, April 2004.

were already present on the insurance market. Products and prices of insurance were initially similar to one another, for they had evolved from shared common origins set by the insurance association. In 1993/94 the first bigger changes occurred, transforming the broad previous "full" KASKO insurance into insurance cover that can be modularly combined.

Table 1: KASKO insurance market data for 2002

Austria	Italy	Slovenia	
Number of inhabitants	8,102,000	85,000,000	1,987,971
Number of all vehicles	5,509,508	42,950,325	1,117,384
No. of cars	4,097,145	33,706,153	876,405
No. of inhabitants / car	1.98	1.72	2.27
No. of insurance companies offering car insurance	24	More than 40	7
No. of insurance companies per million vehicles	4.4	1	7
No. of KASKO insured vehicles vehicles	1/3 of all vehicles	Data not gathered	1/3 of all
Gross KASKO premium	820 million €	Data not gathered	101 million €
Share in property insurance	15%	Data not gathered	13%

INSURANCE MARKET

KASKO insurance market data for 2002 (see Table 1).

INSURED RISKS

Further on, the risks are stated for which the repair of the vehicle is covered by the insurance company, or its value reimbursed in the case of a total loss.

Austria

As a rule, KASKO insurance coverage covers all the risks mentioned below:

– Natural events (lightning, rock falling, landslide or snowslide, hail, storm, flood), fire, explosion, theft, robbery, hitting wild animals, windscreen breakage. In these cases, as a rule, without excess[2].

– Collision, damage due to negligence. In these cases excess is always deducted.

The bonus/malus[3] system is **not** used with KASKO insurance.

Italy

In Italy KASKO as a rule means the following coverage packages:

– The risk of collision only, that is, classic collision with another known participant. Most often under the name of "Minikasko". Almost without exception participation of the insured in the form of excesses and noncoverage[4] is required.

– The full KASKO coverage comprises the following: collision with another participant in the traffic, sliding off the road, overturning, hitting an obstacle. Only exceptionally natural events, socio-political events and malicious acts are also covered. Almost without exception excess (deductibles) and noncoverage apply.

The most widespread form of coverage, that as a rule is not included in the KASKO, and is sold to a great extent together with the liability car insurance is:

– Fire, theft. Almost without exception excesses and noncoverage apply.

The bonus/malus system is **not** used in combination with KASKO insurance.

Slovenia

As a rule in Slovenia the term "full KASKO" means coverage of the following risks:

– Traffic events (collision, sliding off the road, overturning). In these cases the damage caused by car load or objects in the vehicle is covered as well), falling objects, fire, explosion, acts of malicious intent, socio-political events, natural events. Acquisition of coverage with and without excess is possible.

– The risk of theft is most often excluded from the KASKO coverage and presented as an additional coverage.

In addition to the stated combined risks there is an option of partial kasko insurance. These are narrower combinations of risks or causes of damage than the full kasko, which can be acquired together with vehicle liability insurance or with full kasko, so that the bonus is not lost (breakage of lights, glass, mirrors, hitting wild animals, parking lot damage, replacement vehicle...).

The bonus/malus system **is** in use with KASKO insurance, which means that the premium decreases through the years with no claims and vice versa.

BASIS FOR CALCULATING THE PREMIUM

Austria

Two key factors

– "Catalogue" value of the vehicle[5]

– Repair costs of a typical damage according to the type of vehicle (prepared by the insurance association) and

– A number of "soft" criteria applying to the owner of the vehicle – the driver (age, experience, area of usage, mileage, garage, ...)

No recommended rates are suggested by the insurance association or others.

Italy

– Value of the vehicle

– Engine power (cavalli fiscali[6])

– Additional "soft" criteria applying to the owner of the vehicle – the driver (age, experience, area of usage, mileage, garage,...) which greatly influence the cost of the premium, as well as the decision of the insurance company to write the insurance at all.

No recommended rates are suggested by the insurance association or others.

Slovenia

– "Catalogue" value of a new vehicle

– The bonus/malus system (allows for 50% discount on the premium)

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[2] Participation of the insured in paying for the damage, deducted by the insurance company from the paid out insurance money in the sum set out contractually

[3] Reducing or raising the insurance premium when underwriting the insurance depending on claims history in the past insurance period.

[4] Participation of the insured in paying for the damage, expressed in percentage of established damage.

[5] New market value of the vehicle, as determined by a specialised organisation.

[6] Specially formed classes for taxation needs. Used also as a criterion for risk assessment.

– Individual risk assessment for higher price range vehicles. For insuring other vehicles the "soft" criteria have not been used to a great extent yet.

No recommended rates are suggested by the insurance association or others.

COMPETITION

The conclusions drawn in this chapter are based on observation over the past five to ten years.

Austria

Liberalisation of the market in 1994 in the presence of a larger number of insurance companies wishing to increase their market shares caused:

– Price competition (discounts)

– Product competition

– New free of charge coverages are added, excesses abolished, coverages comprise hitting all animal species, not only wild animals, breakage of headlights, short-circuit in electricity, ...

– Additional free benefits

A replacement vehicle, safe driving courses, costs of number plates, costs of the driving licence duplicate ...

Italy

Even with strong levels of competition, Italian insurance companies are very careful when it comes to underwriting KASKO insurance. They mostly opt for writing on the basis of knowing the insured (own clients), they do not give offers without personal contact, premiums are relatively high. In general it is not easy to compare among insurance coverages, participation of the insured, premiums of individual insurance companies and determine which is the better deal.

Information on insurance companies themselves is also not widely available, for example from the ANIA insurance association, which confirms that the market is currently stable, not desiring any particular competition "battles".

Slovenia

– In the beginning of the nineties new insurance companies were formed. A desire to increase the insurance portfolio has been present. The consequences are:

– Price competition (discounts)

– New or changed products are offered (at first with the goal of improving the claims ratio)

– New insurance companies appear, some of the existing domestic ones broaden their range of activities

Italian insurance companies move cautiously when underwriting KASKO insurance cover.

– A consequence are professionally unfounded measures: additional discounts, unjustified bonuses, insurance for new value of the vehicle, ...

– In 1999 the market leader reduces premiums by more than 20%, the other insurance companies follow

For the moment, knowledge that has obviously been present in Italy for a number of years has apparently not become established in the Slovenian market yet.

INSURANCE MONEY ENCOMPASSES

Austria

Reimbursed costs:

– Repair costs, towing costs

– Reimbursement of diminished value[7] of the vehicle is possible.

– When the presence of total loss[8] is established, repair costs are not paid but a replacement value is. The value of the vehicle before the insurance event is calculated on the basis of depreciation[9].

– The previously set excess is deducted from the sum of insurance money, which mostly applies only to the risks of traffic events and damage caused by negligence of the insured.

Italy

Reimbursed costs:

– Repair costs, towing costs. In some insurance coverages depreciation is taken into account in partial damages also.

– Reimbursement of diminished value of the vehicle is **not** possible.

– When a total loss is established, repair costs are not paid but the replacement value is. The value of the vehicle before the insurance event is based on its market value[10].

The previously set excess and noncoverage are deducted from the sum of insurance money, which applies to the majority of insured risks.

Slovenia

Reimbursed costs:

– Repair costs, towing costs, costs of damage caused in preventing additional damage (extinguishing fire, prevention of sliding into a precipice ...), costs of damage due to precipitation immediately upon the damage event

– Reimbursement of diminished value of the vehicle is **not** possible

– When the presence of a total loss is established, repair costs are not paid but replacement value is. The value of the vehicle before the insurance case is based on depreciation or market value.

The previously set excess is deducted from the amount of insurance money, which applies to the majority of insured risks.

A claim results in the loss of bonus only in some risks.

ENVIRONMENT

Austria

– Increase of repair costs by 4 to 5 % annually (hourly labour rates amount to 70 € and more)

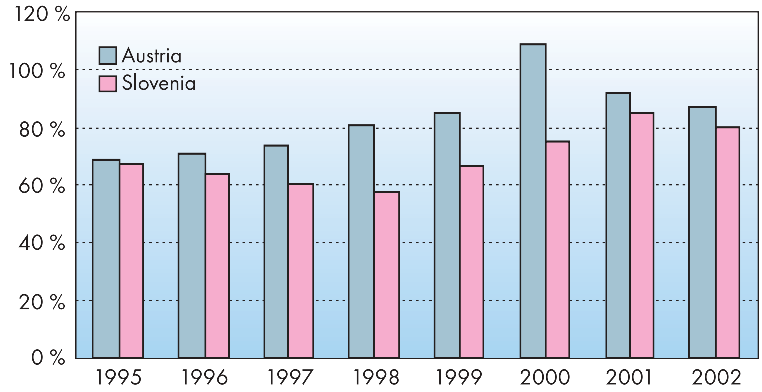
[7] Reduced value of the vehicle due to repaired parts without identical characteristics to those before the repair.

[8] Total loss presents a damage case where repair costs and value of salvaged parts of the vehicle exceed the value of the vehicle before the damage case.

[9] Loss of value of the vehicle due to economic and tehnical wear and tear.

[10] Value, achieved on the market by a group of vehicles of the same make, type and equipment.

Figure 1: KASKO direct claims ratio



Data do not include costs.

– Cost of repair for the same damage strongly increasing

Mirror replacement for Golf I = 40 € and Golf V = 475 €

– The "maximum repair" mentality is present (new parts when this is not necessary, lacquering a larger surface than necessary, ...)

– A tendency to insure the full kasko (due to low prices)

– A tendency toward contracts written for a longer period of time to keep premiums low

Italy

– Increase of repair costs above the inflation (hourly labour rates amount to €30 to €50)

– Cost of repair for the same damage strongly increasing

Mirror replacement for Golf I = €40 and Golf V = €375

– Insurance companies adjust the premium according to the claims history, so there is no special pressure to write contracts.

The array of insurance products is wider in Austria and Slovenia than in Italy.

Slovenia

– Increase of repair costs by 8 to 10 % annually (hourly labour rates amount to €40 and more)

– Cost of repair for the same damage strongly increasing

Mirror replacement for Golf I = €30 and Golf V = €292

– The "maximum repair" mentality is present (new parts when this is not necessary, lacquering a larger surface than necessary,...)

– The tendency to insure the full kasko without excesses (due to low prices)

– Unjustified granting of bonuses or insufficient checking when the insured transfer to other insurance companies

– The presence of insurance fraud, which is due to inappropriate (not content-oriented) court proceedings not adequately sanctioned

RESULTS

A consequence of the state of affairs in the insurance market can be seen in the review of the direct claims ratio. The latter represents the ratio of claims paid to gross premiums collected in the year observed, not taking into account transferable premiums and claim reserves. The information for Italy was unfortunately not available.

Results of the figures posted for the observed period undoubtedly confirm findings stated in the previous chapter. Undisputedly in Austria in 2000 certain measures were undertaken that have the effect of gradually improving the claims ratio. In Slovenia this is obviously not the case, for the trend has been negative since 1999. For successful operation of insurance companies, direct claims ratio can amount up to 70 percent at most.

In 2000, the measures implemented in Austrian insurance gradually improved the claims ratio. Unfortunately, Slovenia has not been

Figure 2: Trend of claims ratio A

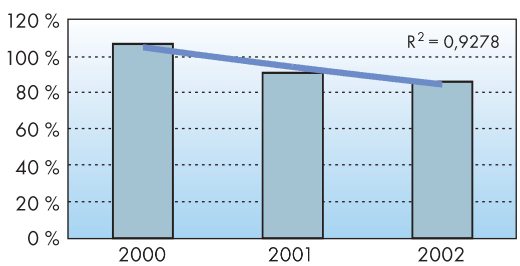
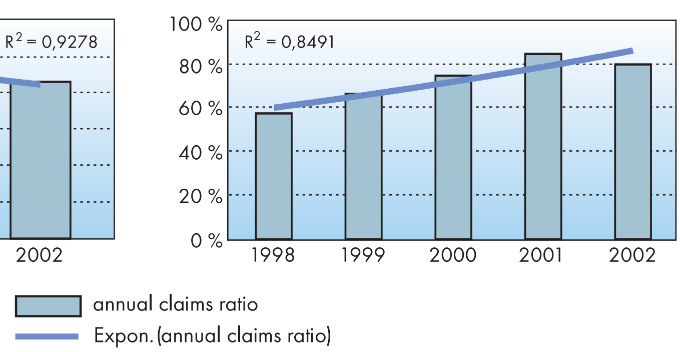


Figure 3: Trend of claims ratio SLO



successful in this field as claims have been exceeding premiums written since 1999.

COMPARATIVE FINDINGS

In all countries observed the insurance market of the KASKO insurance is well developed. The extent of insured risks covered by individual coverages is similar in Austria and Slovenia. A quite broad coverage with limited application of excess is offered. In Italy coverages are often not so broad, the sales are more discreet and selectively oriented, a participation of the insured in the form of excess and noncoverage is always present.

Penetration – market coverage in Austria and Slovenia encompasses a third of all registered road motor vehicles. In Italy vehicles are insured in a greater number for the risks of fire and theft only, whereas KASKO is less widespread. In Slovenia, seven insurance companies per a million vehicles write KASKO insurance, in Austria 4.4 insurance companies operate per million vehicles, in Italy only one.

Strong competition and a desire for portfolio increase is reflected also in the claims ratio, which in Austria is gradually improving after several negative years. In Slovenia a need for taking action has not been recognised yet, despite the negative trends, whereas in Italy the selectivity and high price have been present in selling this insurance for a number of years, which is reflected in a successful claims ratio.

The major differences between the countries lie largely in the theoretically possible size of the insurance portfolios. In comparison with Austria, Slovenia has a quarter of the number of inhabitants and a fifth of the number of motor vehicles, and in comparison with Italy one fortieth of the number of inhabitants and the same ratio of motor vehicles.

CONCLUSION

Slovenia does not lag behind in any respect with regard to KASKO insurance of road motor vehicles in comparison to its neighbours Austria and Italy. Coverage of the market is according to some criteria even greater than that of its neighbours, a range of choice of insurance coverages is at least at the same level, while the insurance premiums are significantly lower. Competition among insurance companies is still present, allowing the insured to choose a broad coverage with low insurance premiums.

Unlike in the neighbouring countries, the claims ratio in Slovenia still shows negative trends, which Slovenian insurance companies still fail or refuse to take into account.

Due to its smallness, the current claims ratio for KASKO insurance, and a big concentration of insurance companies, the Slovenian insurance market is certainly less interesting for new insurance companies. It can be foreseen, that despite the difficulty of returning the investment, several new insurance companies will decide to write KASKO insurance, mostly with the intention of offering a full range of insurance to their clients.

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Dilemmas and Opportunities of Voluntary Health Insurance

*Marko Jaklič**

DILEMMAS AND OPPORTUNITIES OF VOLUNTARY HEALTH INSURANCE
Demographic problems, such as birth rate drop along with prolongation of life, are the most acute problems in a modern social State. The circumstances in Slovenia are fully comparable with those in European countries: population is getting older and as a consequence, higher health care costs may be expected. Considering the existing deficit in the compulsory health insurance scheme, growing health care expenses and some problems in the area of complementary health insurance, changes in the Slovene current health care system have to be made. Furthermore, increased costs for health services and pharmaceuticals in last few years have brought complementary premium rate up to the limit that could hardly be exceeded as it already represents high expense to the poor. The success of our country in the future will depend a lot on efficient adjustment of the public sector that also includes health care, so Slovenia has to combine public and private financing in such a way that it would provide a long-term stability of the health care financing system. In the area of complementary health insurance an important aspect of its long-term stability is the implementation of risk equalization schemes that provide stability of the community rating based complementary health insurance. Without the equalization, insurance companies are stimulated to select "good" risks and to avoid "bad risks", which can be harmful for the long-term stability of the whole medical system.

For most European Union (EU) member states the problem of ensuring health security is an object of numerous discussions and detailed study. From year to year, the crises of health systems are deepening, and because of the influence of "medical inflation", the most important factors of which are new medical technology and demographic changes, the public health fund deficit is increasing annually. Wishing to maintain an economically competitive position, the market economy countries are forced to reflect upon how much of the public resources, collected from contributions or taxes, can be spent on health care, how private funding could be attracted and how available resources could be best distributed to ensure long-term quality, accessible health security for the whole population. Here, Slovenia is no exception. Health Insurance Institution of Slovenia (HIIS) providing compulsory health insurance in Slovenia registered last year a loss of 11 billion Slovenian tolars, which is by some predictions going to grow to 70 billion by the year 2008. Some important systemic issues with regard to voluntary health insurance also remain unsolved.

Funding health care

The Slovenian system of health insurance is based on Bismarck's social model. The system has gone through several reforms. 1992 represents an important turning point in the development of Slovenian health security, when essential systemic changes were made - the concept of national health security provided by the state was abandoned and the system of

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compulsory health insurance operated by the then newly established HIIS was introduced. This substantially changed the structure of financing – namely, in 1991 98.5% of health care funds was collected through taxes, while only one year later the main financial source was compulsory health insurance[1] . After the 1992 reform, the package of services covered by compulsory health insurance remained very broad, covering almost all services, but additional payments for some services were introduced (at the same time, participation of the insured as required under the previous system was abolished). For some groups of insurants and for some diseases, the services are covered entirely by compulsory health insurance, in some cases the insured participate with additional payments, expressed as a percentage of the price of the service[2] . They can pay the additional payments by themselves or in order to avoid additional payments obtain supplementary health insurance, which was introduced in 1993.

The reason for introducing voluntary health insurances, including supplementary health insurance, was the desire to increase the number of sources for financing health care. This is the reason why they were heavily promoted by the government, even though there was a fear that this could lead to a parallel system of health care. Predictions about introducing supplementary health insurance were rather cautious, since the government estimated that it would be introduced gradually and that approximately 300,000 citizens would be insured in the first year of the supplementary health insurance being offered. In fact more than 1.3 million people obtained insurance in the first year. This was because of the fact that supplementary health insurance was introduced along with changes in the social system in a period of considerable uncertainty, and fairly low premiums made it affordable to a wide range of people.

Today more than 1.4 million[3] people, representing 90 to 95 percent of those bound to pay additional payments for health services, are insured with insurance companies marketing supplementary health insurance.

Since 1993 voluntary insurance took on an increasingly more important role in financing the health care system, since, among other things, additional payments that were legally set in spans, increased with time. In 1993 less than 7 percent of health care funding was obtained through voluntary health insurance. Gradually this share increased and in 2001 amounted to 15 percent, and stayed approximately the same in the following years as well (*Figure 1*). The share of funding from supplementary health insurance in total resources for financing the health system increased due to an increasing share of additional payments as well as quickly increasing costs of medicines. Medicines are largely paid from supplementary health insurance, and medicine expenses account for almost a half of all expenses .

Despite significantly contributing to the stability of Slovenian health care system, supplementary health insurance in the past decade could not avoid some problems. Increases in the costs of medical services and pharmaceuticals in particular caused premiums to rise to the level where it is increasingly becoming too high for some individuals. Such development was to a great degree driven by HIIS, when it systematically transferred expenses from compulsory to supplementary insurance by reducing the portion of coverage of the compulsory insurance and by rearranging medicines on the lists. Increases in additional payments would be smaller if the contribution rate were adjusted to increased needs for health care services. By shifting costs to supplementary health insurance

Figure 1: Share of compulsory and voluntary insurance in financing health care

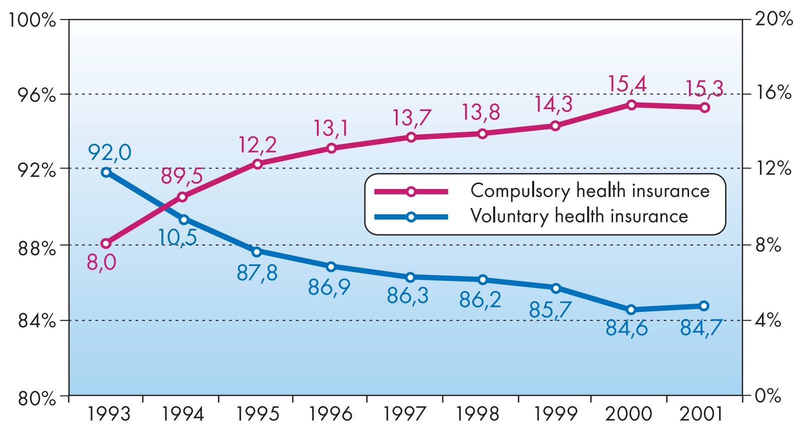
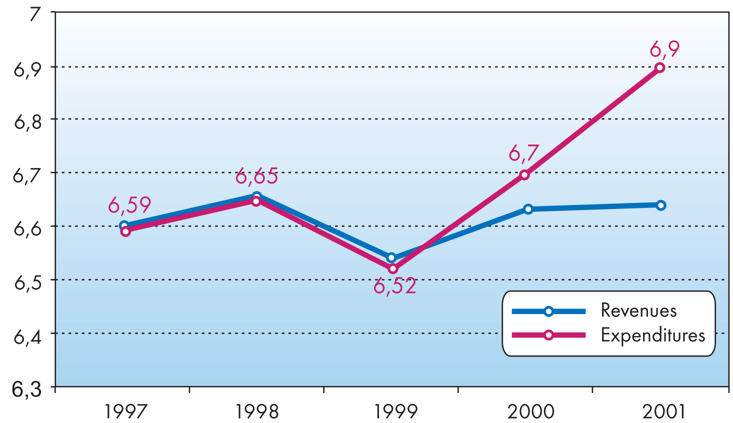


Figure 2: Revenues and expenditures in compulsory health insurance as a percentage of GDP



[1] Contribution rate from 2002 on amounts to 13.45 % of the gross earning – employees pay 6.36 %, whereas employers pay 6.56 % and an additional 0.53 % for coverage of work-related injuries and illnesses.

[2] Additional payments can be lower than 5 %, for example for the most demanding surgical procedures, from 15 to 25 % for most hospital services, 25 % for pharmaceuticals on the positive list, and up to 75 % for pharmaceuticals on the intermediate list.

[3] From this 1.2 million or more than 80 percent are insured with Vzajemna, approximately 250,000 with Adriatic, whereas Triglav health insurance company started to market these insurances last December, so there is no official data on the number of their insurants.

and as a consequence increasing the premiums for supplementary insurance, HIIS was able to balance its own expenses and keep the compulsory insurance contribution rate unchanged. This is precisely why premiums for supplementary insurance increased more quickly than total earnings, which is the basis for calculating compulsory health insurance contributions *(Figure 2)*. From the year 2000 premiums increased also due to a modification to the *Health Care and Health Insurance Act (HCHIA)* from 1998, which required building up of old-age reserves for supplementary health insurance.

Legal changes or inconsistent legislation have otherwise caused quite some problems in writing supplementary health insurance. The basic acts regulating supplementary health insurance, HCHIA and *Insurance Act*, define supplementary insurance differently. HCHIA defines supplementary health insurance as long-term risk insurance, where old-age reserves must be accumulated. However, when introducing the demand for building up reserves, the state did not attend to those generations that had not created them in the past (it is estimated that this financial gap amounts to 200 billion tolars). The two insurance companies present in the supplementary insurance market at the time could not raise premiums to the extent of ensuring coverage of the gap in a short period of time. If the state, when it introduced risk insurances, had also taken care to fill in the "reserve hole", insurance companies could write pure risk insurances today.

On the other hand the Insurance Act defines supplementary health insurance as public interest or as mutual, solidarity insurance, with a premium that is approximately equally high for all, irrespective of the risk. Since supplementary health insurance can be written by mutual insurance companies as well as by limited companies, big differences in portfolio structures with regard to the age of the insurants arise. Deficient legislation allows unreal competition, stemming from allowing an individual insurance company to acquire a more advantageous portfolio structure with regard to age and health status of insurants. With an advantageous structure of insurants the insurance company can offer a lower uniform premium or achieve a better result than the competition, which is unacceptable from the public interest viewpoint. The Act does demand that insurance companies accept anyone who wishes to obtain supplementary health insurance under the same conditions. However, insurance companies have enough opportunities for selective marketing of the insurances, which also yields a disproportionate distribution of insurants in insurance companies with regard to risk. In the long run this could lead to instability of supplementary insurance, so the Insurance Act from the year 2000 determines it as public interest and states that all insurance companies marketing such insurances must be included in risk equalization schemes to equalize the differences in the costs of health services stemming from differences in age structure, gender structure and structure of severely ill. Four years after adopting the Insurance Act, an act that would appropriately regulate the equalization schemes still does not exist (that equalization schemes are in accordance with EU legislation, was last year also confirmed when the European Commission approved the Irish model of risk equalization schemes, on which the Slovenian proposal is modelled[4]). Insurance companies have been bringing to attention these problems which significantly affect writing of supplementary health insurances for a number of years.

Health care reform

In 2003, the Ministry of Health addressed some health care problems by presenting a health care reform draft, in the framework of which a large part was dedicated to a thorough reform of the health insurance system. In the draft of the reform it was foreseen that supplementary health insurance would again be incorporated into compulsory health insurance (with an increased contribution rate), which would significantly change the ratio between public and private health care resources.

This ratio otherwise in Slovenia is quite comparable with the average ratio in EU15, where the scope of public funding ranges from 60 to 80 percent, which, according to the experience of these countries, is an optimal combination of both sources of funding. After the suggested change the mentioned ratio would be different in Slovenia: the share of public funding would increase from the present 76 percent to more than 90 percent. The share of public funding in financing health care in Slovenia would thus become significantly higher than in most European countries, voluntary health insurance would be reduced to a minimum. Slovenia would be an exception in the European area, for in most countries due to increasing health care costs, public expenditures are being cut, while the share of funds to be paid for medical treatment and medicines from the people's pockets is increasing. The solution offered by the Ministry of Health, would, as some macroeconomists have estimated, affect the the country's macroeconomic situation by fuelling inflation and hampering export competition and thus lead to an ailing economy. This is also important as we are attempting to cut inflation to a level that would enablea "trauma-free" entry into the ERM 2 exchange rate mechanism.

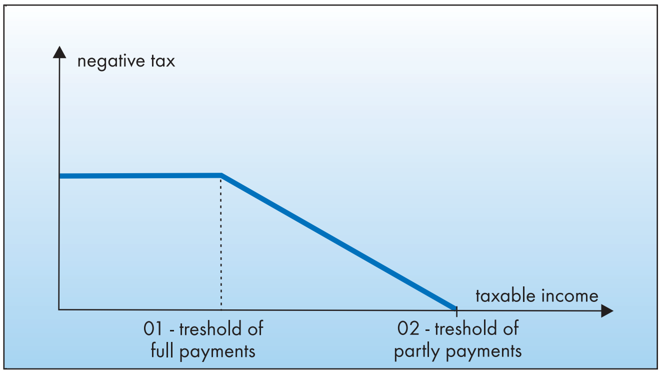
The reason for making supplementary insurance compulsory is claimed to be increased accessibility – due to excessively high supplementary insurance premiums, a certain part of the population is said to be not using the services of the public health care system. However, premiums are not too high for the majority of the present insurants, and at the same time the present method of calculating the premium overcomes anomalies in compulsory health insurance which allow some groups of insurants to "take advantage" of the system at the expense of others.

Therefore, the state should only take care of the needs of that part of the population which really cannot afford supplementary health insurance premiums due to low total income and the economic situation with health care reform. Instead of the abolition of supplementary insurance as proposed in the reform, introducing a so called "negative tax" with this insurance as a social adjustment measure, calculated on the basis of the income tax return, would be significantly more efficient

[4] http://www.euireland.ie/news/comp/0503/irishhealthinsurance.htm

and rational *(Figure 3)*. According to this proposal, all insurants who wished to do so would pay for supplementary health insurance at the same amount as before which would continue to ensure solidarity among the healthy and the ill, the young and the old. When filing the income tax return, health insurance premiums would also be included in the report. Citizens with low incomes (below the annually set poverty threshold) would benefit from having a negative tax taken into account, or the supplementary health insurance premium regarded as prepayments of income tax. This tax would increase at a flat rate from the poverty threshold downwards or increase up to the premium sum, and above the poverty threshold it would amount to zero. The described proposal takes into account total income, reported in personal income tax report, which is also in accordance with the goals of the new fiscal reform, which will encompass all revenues of an individual as the new legislation comes into effect. It would have to be determined how quickly the negative tax would increase with the lowering of taxable income. It would make sense that below a certain taxable income set in advance it would be as high as the premium – so that health insurance would be fully covered for the most poverty-stricken inhabitants. Such a model would not cause secondary macroeconomic effects in the labour market or bring about the rise of inflation, but it does maintain the option of obtaining supplementary insurance - truly following the principles of a social state - and provides citizens living below the poverty threshold with a subsidized supplementary health insurance.

Figure 3. Negative tax as social adjustement with supplementary health insurance.



In the process of public debate the original proposal of health care reform did not gain support. The Strategic Council for Health Care Reform appointed by the Government at the end of February this year confirmed the premises for a (new) model that would still preserve the supplementary health insurance and thus the majority of private resources within the health care system, but would introduce significant changes. According to this proposal, supplementary health insurance premiums would depend on the total income of an individual or an individual's ranking into an income class. The ratio between premiums in classes would be established by a legal act, according to the first proposal in the ratio of one to five. Income thresholds would be legally established, below which citizens were exempt from additional payments and thus from supplementary insurance (it is estimated there would be approximately 170,000 of those). For uninsured persons, a maximum annual amount of additional payments would be set, which would depend on the income class of the person. The proposal also foresees abolition of old-age reserves. The Ministry of Health expects greater control or regulation of supplementary health insurance from this proposal. Thus it would give consensus to issuing permits for writing these insurances, and also regulate the maximum loading tega ne zastopim!!!.

The proposal is nowhere near being implemented, for there is a lack of clarity with regard to a number of issues pertaining to it. Judging from the data collected so far it is specifically not clear as to who would have to pay additional payments, and which persons would be exempt from it. Uncovering information about an individual's income is also questionable, for insurance companies would obtain access to this information (and since they would be carrying into effect "the maximum annual amount of additional payments", it is most likely the providers of health care services would obtain access to this information as well). Due to large differences in premiums there is a high likelihood that a part of the population with higher income would not opt for obtaining insurance, which could cause instability in the system. Differentiating premiums according to income also raises the question of the equalization between different risk groups. Already at the moment, problems occur in providing supplementary health insurance, since the average claim costs per insured of one insurance company are lower than of another, due to different portfolio structures and the fact that average annual health service costs are several times higher for older insurants than for younger insurants. If differentiated supplementary health insurance premiums were introduced, this problem would escalate, since this would change the structure of revenues for the insurance companies, but the structure of expenditures would not be changed. This would hinder or wholly prevent implementation of equalization schemes and cause a number of additional problems. Moreover, a dependence on premiums based on income would be an exception in EU. Some claim that such a system is known in France – but theirs is significantly different: there the insurance company calculates the premium on the basis of the age of the insured, and then only when it comes to group insurance, discusses with companies in what way the premium will be paid. If an employer decides sponsor the premium in part or wholly in dependence on earnings, the company qualifies for atax relief.

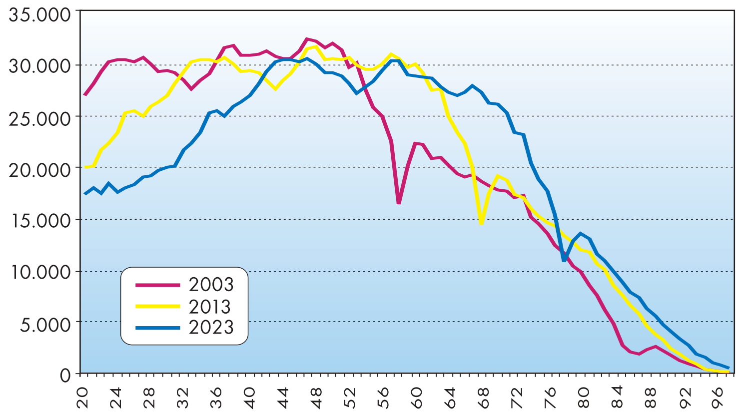
Bundle of Rights

In addition to the pending changes, a definition of the basic package of services to be covered by the compulsory health insurance is surely of utmost importance. For historical reasons, this package in the case of Slovenia is very rich and encompasses essentially all services. However, at the same time such rights are often rights only on paper, for the insurants cannot take advantage of them because of too little capacity or too scarce resources, which create long waiting lists. Such organization also allows little room for manoeuvres to introduce other forms of voluntary insurance that could relieve the pressure on public funding to a certain extent. Despite the unpopularity of reducing rights stemming from compulsory insurance, such measures will be inevitable sooner or later. In the world today there is not a system offering citizens all rights, of high quality and without additional payments. Reforms in other countries are also going in the same direction – the German health care (pre)reform in 2003 for example abolished social compensations (funeral expenses, death benefits), payment of a part of dental services for adults, and payment for the majority of optical appliances, it caused the transfer of an obligation to pay a premium for sick-leave to insurants, in most cases ceased paying travel expenses, increased additional payments to be paid by insurants, and implemented other measures for cutting the costs of health funding. In Slovenia we will first have to precisely define the bundle of rights arisingfrom the compulsory insurance, for only this will enable us to develop other forms of voluntary health insurance. For these, as with all other insurances, there must be risks that potential insurants carry. If there is no such risk, there is also no reason to get insured.

Not only Slovenia, but other members of EU are also dealing with the question of health security and reform of the system. They too, like Slovenia, are encountering problems in ensuring funds for health care, also due to negative demographic trends. Population trend projections show that the number of inhabitants will not significantly change in the following years, but the share of those older than 65 years of age will increase – in twenty years by half *(Figure 4)*. If there is no significant influence of migrations, in twenty years the number of young people aged 20 to 35 will be 30 percent lower than now. Decreases in the number of young people will continue to lower the birth rate, which can have further negative effects on the demographic structure. Statistically, the population of Slovenia has "grown older" by four months each year in the past five years.

EU states are realizing that they will not be able to carry the burden of ensuring health security from public resources in the long-term by themselves, and therefore are reducing the share of public funding and increasing participation of the individual. Similarly, Slovenia will also have to find an appropriate balance in funding health care, so that at least the same level of health security

Figure 4: Projection of the age profile of Slovenian population until 2023



will be ensured for citizens in the future as it is today. This can be partially accomplished by changes that do not significantly change the system and can be implemented simply and quickly. One of these is an exact definition of the bundle of rights to be ensured by the compulsory health insurance, whereby it is necessary to open up possibilities for encouraging a bigger share of private resources in funding health care. Also, a compromise solution will have to be formed as soon as possible to solve the problem of those who cannot afford to pay supplementary insurance premiums. Since supplementary health insurance will certainly play a very important role in the Slovenian health care system for some time, it is most necessary to ensure its long-term stability by introducing equalization schemes.

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Credit Insurance

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CREDIT INSURANCE

The unique status of credit insurance is not only a characteristic of the Slovene insurance market but is the situation present worldwide. Thus for insurance companies dealing with credit insurance, entering the Slovene market will not represent different environment but rather similar market opportunities as in their local markets and competition with similar products. As far as these are concerned almost 95 % of traditional marketable export and domestic credit insurance is in portfolio of Slovene Export Corporation dealing also as the authorised institution (Export Credit Agency) with nonmarketable credit insurance on behalf of and on the account of the Republic of Slovenia. On the other hand Triglav Insurance Company credit insurance portfolio consists of mainly consumer loans, while other types of credit insurance as well as other insurance companies do not play a significant role. Bearing in mind relatively high market penetration, taking over the existing portfolio in different forms or approaches might be of interest especially for the mayor players among credit insurers. Finally the article attempts to predict some future development within the credit insurance industry in Slovenia and its pros and cons in view of Slovene accession to the European Union.

According to the title of the article, the reader may expect it to deal with various forms of credit insurance, of which the credit insurance/security offered by insurance companies can be only one possible alternative way of transferring or decreasing risks. The purpose, however, is not to describe various types of corporate and personal security, although they do represent a serious and considerable competition to the services provided by insurance companies. Our intention was to present – in the context of other insurance types and activities of insurance companies – the specific features of credit insurance, the current situation and expectations in view of Slovenia's accession to the European Union (EU).

Like elsewhere in the world, in Slovenia also, credit insurance represents only a small segment of the overall portfolio of insurance companies, but in absolute terms it is not insignificant.

This article speaks about credit insurance provided either by multi-line insurance companies or by specialised credit insurance companies. The term credit probably needs no specific explanation. However, to understand the term credit insurance it seems relevant to explain what it usually covers: the most important are the receivables arising from sales on deferred payment terms and the related loans extended by financial institutions. On the other hand, any other risks listed in Article 2, paragraph 2, point 14 of the Insurance Act (Official Gazette of the Republic of Slovenia, Nos. 13/00, 91/00, 21/02 and 50/04 (ZZavar)) are not relevant

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in their scope. In addition to credit insurance, companies in Slovenia provide also cover against mostly sales-related risks, such as insurance of pre-shipment risks, CAD transactions risks, etc. Insuring of investments and (non)shareholder loans, usually an activity of state-supported credit insurance companies, is not a subject matter of this article, however, some characteristics of non-marketable credit insurance listed in Chapter VI apply also to these types of insurance.

Credit Insurance in Slovenia

Credit insurance has a long tradition in Slovenia, however, it has never had an important position in the business of insurance companies[1] . And even when it had a more significant role – in particular in the first half of the 1990s – it proved negative for insurance companies and resulted in many insurance cases and high indemnities. This critical period was followed by years of stagnation and consolidation of portfolios, adopting new approaches to risk assessment and abandoning or restricting certain subtypes of credit insurance (notably, insurance of financial credits).

Consumer loans approved by banks and other financial institutions to natural persons have preserved the leading role in credit insurance. In the early 1980s and before that, consumer loans were largely approved by companies (in those times, however, having a different status) dealing with the sales of consumer goods. However, a decade and more ago, this trend turned more in favour of banks, largely as a result of an aggressive policy of the banks and also for purely practical reasons, i.e. the possibility to check the liquidity of credit-takers. If we use the terminology applicable to trade credit insurance, the buyer credit scheme prevails over supplier credit scheme, which involves the seller selling on deferred payment terms and the buyer. According to the data of the Slovenian Insurance Association, consumer loans accounted for almost 57 % of the overall credit insurance portfolio in 2002, which makes this the most important type of credit insurance.

Despite what has been stated above, this article focuses largely on trade credit insurance, i.e. insurance against risks related to the sale on deferred payment terms between legal entities. Although Triglav Insurance Company has the longest tradition in this area, having started to provide export credit insurance in Slovenia back in the mid-1960s, today the leading position is held by Slovene Export Corporation, holding an almost 95 % share (2002, data from Slovene Insurance Association) in the Slovenian market. It is a specialised financial institution with credit insurance as its main activity, which means that it is focused largely on this insurance product and strives to develop overall quality services for its clients.

Consumer credits have had a leading role in credit insurance and still do.

The future development of credit insurance services will probably be the most dynamic in specialised credit insurance companies, as they will be able to provide services tailored to the expectations and requirements of their clients. On the other hand, there are certain advantages of multi-line insurance companies in their offering of credit insurance, such as an opportunity to provide comprehensive property insurance for a legal entity. However, such comprehensive insurance brings about also certain well-known threats: the pressure to conclude other non-life and personal types of insurance, which means higher earnings for insurance companies, be it in % or in absolute terms. In this context, the basic principles of sound insurance practice may be disregarded when an insurance company provides credit insurance on terms which do not match the degree of risks. It cannot be claimed that such a situation is typical for Slovenia in the area of credit insurance, but individual cases cannot be excluded. Providing credit insurance in specialised insurance companies eliminates these potential risks typical of the multi-line insurance companies, because of the insufficient division of authority and the lack of what is known as a Chinese Wall.

According to data from the Slovenian Insurance Association, there are seven insurance companies operating in the Slovenian credit insurance market, of which Triglav Insurance Company and Slovene Export Corporation are the most important[2] . This means that there is a certain degree of competition present in Slovenia, which is even further strengthened by the presence of foreign insurance companies (in particular in the area of export credit insurance) offering their services to Slovenian companies, largely those in majority ownership of foreign legal entities and usually through their foreign owners.

Credit Insurance in the EU

Some EU Member States have a long tradition in credit insurance, sometimes even longer than a century. In 2003, the International Credit Insurance and Surety Association (ICISA) celebrated its 75th anniversary, whilst the history of another large association - the Berne Union (International Union of Credit and Investment Insurers) dates back to 1934. The members of the Berne Union, of which Slovene Export Corporation is also a member, recorded premium revenues totalling USD 4.25 billion in 2002, and they insured business transactions worth USD 485 billion.

[1] According to data from the Slovenian Insurance Association, the credit insurance premium accounted for only 2.2% of total collected gross premium in 2002, and according to the Insurance Supervision Agency, the gross credit insurance premium accounted for 4.3 % of total non-life insurance premium (except health-care insurance) in 2002.

[2] According to data of Triglav Insurance Company and Slovenian Insurance Association, Triglav had around 66% market share and Slovene Export Corporation 17 % market share in the area of credit insurance in Slovenia in 2002.

In the EU, credit insurance is largely provided by credit insurance companies and only rarely by multi-line insurance companies. In particular in small markets, the latter hardly hold more than negligible shares. Like any type of insurance, credit insurance also requires a certain volume of business to be managed rationally and profitably. Therefore, credit insurance companies tend to merge. Today, there are only three important large credit insurance groups: Coface, Euler Hermes and Atradius (former GERLING NCM). All other companies have a regional character and use their national affiliation and acquaintance with the local market as their comparative advantage. However, the competition imposed by large groups is increasing even in these local markets. By expanding their services (apart from insurance, credit rating reports and debt collection activities also) and by a rapid responsiveness it will not be difficult to obtain new clients, even more so because the product of trade risks insurance, be it domestic or export, will also further improve.

What was said in the previous paragraph relates largely to insurance of domestic and export trade credits against commercial and non-commercial risks in countries where capacities of reinsurance market are available. Unlike in Slovenia, export credit insurance (including receivables between economic subjects within the EU) represents the highest share in the insurance portfolio of credit insurance companies. Other types of credit insurance, such as consumer credit insurance, for instance accounted for only 1.3 % of total insurance portfolio of Euler Hermes in 2003. The situation is similar in other credit insurance companies, many of which have even abandoned consumer credit insurance because of poor results achieved in the past. Today, suretyship insurance and fidelity insurance represent larger shares than consumer credit insurance[3].

Preparedness of Slovenian Insurance Companies for Membership of the European Union

By deregulation of Slovenian insurance market, comprehensive EU regulation in the area of insurance has already been implemented. The last amendments to the Insurance Act (Official Gazette of the Republic of Slovenia, No. 50/04 as of 6 May 2004, entering into force as of 7 May 2004) enforced the last necessary adjustments of the national legislation to the *acquis*.

Even before that, insurance companies in Slovenia stressed their high degree of preparedness for accession to the EU in terms of competition, also in the area of credit insurance. Their preparedness is reflected in the level of development of individual products and the quality of services. After decades of development, adjustment to the specific features of Slovenian market and also taking into account the negative experience of the late 1980s and early 1990s, consumer credit insurance has reached such a level of development that it cannot be threatened by competition from foreign insurance companies, at least not without a greater presence on the Slovenian market. Consumer credit insurance requires specific knowledge of local environment, habits of the people, potential sources of information taking into account the regulations on the personal data protection, and in particular, adequate staffing for dealing with claims and pursuing numerous recovery procedures.

Older EU Member States boast over a 100-year long tradition in the area of credit insurance.

If the above estimates are true for insurance of consumer loans (and their variations, such as transaction account overdraft insurance, credit card claims insurance as well as housing loans), the situation is different in the preparedness of Slovenian insurance companies in the area of insuring short-term domestic and export trade credits. In the above-mentioned three largest insurance groups, the degree of development of products/services is higher, in particular with respect to IT services. Given the limited scope of trade credit insurance in Slovenia because of the size of its economy, only Slovene Export Corporation, holding 95 % share on Slovenian insurance market, to some extent follows the trends in the EU. Slovene Export Corporation insures trade receivables between domestic legal entities as well as receivables of Slovenian exporters to their buyers abroad on comparable terms as foreign credit insurance companies. Moreover, it provides information on company credit ratings, debt collection services and through affiliated persons it also provides factoring services to their clients as well as to other legal entities and entrepreneurs. Bearing in mind the cooperation with similar organisations in the EU and knowing their practices, Slovene Export Corporation today – on the conditions applying to it on the reinsurance market – applies the EU regulations even closer than numerous state-supported credit insurance companies or export-credit agencies in the old EU Member States. This is particularly true in respect of the Communication of the European Commission 2001/C 217/02, OJ C 217 as of 2.8.2001. For instance, Slovene Export Corporation for several years has been insuring the exports to buyers from the new EU Member States on its own account and with adequate reinsurance by reinsurance companies, whilst on the other hand certain export-credit agencies in the EU still insure such short-term exports on the account of their states.

Credit Insurance after Accession to the EU

Slovenia's accession to the EU might cause certain changes in credit insurance. First, it means

[3] For example suretyship insurance and fidelity insurance accounted for 3.3 % and 3.5 %, respectively, in the portfolio of Euler Hermes insurance company in 2003.

greater competition from foreign service-providers. Should the interest exist, this will no doubt bring some positive effects at least for clients. The issue of interest is, however, questionable in the area of credit insurance. Because of some negative experiences in the past in Slovenia as well as elsewhere in Europe, one cannot expect any particular expansion in offering consumer credit insurance from abroad. On the other hand, foreign insurance companies might show greater interest in offering insurance for short-term export and domestic trade credits. Competition will increase in particular in the event of a rise in foreign investments in Slovenia. In the case of foreign investment, a parent company usually requires its subsidiary companies to enter into insurance with the same insurance company as itself, because in this manner they achieve lower premiums due to the greater volume of insurance.

In any case, it is more probable to expect an increased direct offer of credit insurance from abroad than, for instance, takeovers of the existing insurance companies. Other types of insurance and their market shares will be more decisive for potential takeovers in Slovenia, as well as potential affiliations in other countries. On the other hand, there is great interest in cooperation with specialised credit insurance companies. Apart from Slovene Export Corporation and the future newly established credit insurance company, there are no specialised credit insurance companies in Slovenia, therefore the latter in particular will be of interest to the three greatest credit insurance companies, largely because of its market share, acquaintance with the market and relatively experienced staff. For example, a representative of EULER HERMES insurance company has already expressed an interest in Slovenia and Coface (at least within CreditAliance) has reported a similar expansion strategy[4]. Given the opportunity for direct operations from abroad, this seems to be sufficient in the first phase for the largest insurance companies, of course provided that there is good IT coverage of the Slovenian market. However, if the insurance portfolio increases later on, all options remain open.

Given the overall trend of Slovenian companies looking for various forms of affiliations and strategic partners abroad, the field of credit insurance is no exception. The newly established credit insurance company may be expected to freely choose a suitable partner and various forms of cooperation, however, the majority ownership structure of Slovenian legal entities can also not be excluded. It would namely allow a specialised provider of credit insurance services to pursue relatively independent and efficient future operations in the enlarged EU market, despite its formal non-affiliation with the three largest credit insurance companies.

Competing credit insurers in the EU will certainly have some impact on operating results, and at the same time the market expansion will offer opportunity to expand.

Non-Marketable Credit Insurance

Discussing credit insurance without at least mentioning non-marketable credit insurance would not be complete. The Slovenian insurance market has been familiar with this type of credit insurance since 1992, when the Act on Corporation for Insurance and Financing Exports of Slovenia was adopted (Official Gazette of the Republic of Slovenia, Nos. 32/92, 37/95, 34/96, 31/97 and 99/99), whilst the new Act on Insurance and Financing of International Business Transactions (published in the Official Gazette of the Republic of Slovenia, No. 2/04 (ZZFMGP), applying as of 14.2.2004) today explicitly states and defines the term non-marketability.

The non-marketable risks, which are, according to market principles, not covered by insurance companies, cannot be defined once and for all. The definition is variable and depends on the conditions in a country and other changes affecting the degree of risks. ZZFMGP in Article 2 defines non-marketable risks as risks which, according to the applicable legislation, the private reinsurance sector is in general not prepared or able to cover because of their type and nature, location, duration and other characteristics. As a result of this and because of the need to provide economic security and competitive conditions of insuring adequate international business transactions of Slovenian economy, these risks are assumed by the Republic of Slovenia.

Non-marketable risks comprise commercial and non-commercial risks. Commercial risks, as described by Dr. Miran Jus in one of his early works[5] and papers on credit insurance, include various events of loss or actions, which occur for one business partner or another because of subjective reasons on the side of the debtor and prevent him or make it difficult for him to meet the obligations. These risks may stem from the debtor's moral values or business habits and result in the debtor not wanting to correctly or fully meet his obligations. In addition, non satisfaction of a debtor's obligations may result from inadequate business activ-

[4] By affiliating with foreign credit insurance companies, additional services can indeed be expected to be introduced, but at the same time, certain functions (underwriting, development of services) will be transferred abroad and a reorganisation of staff may therefore be expected with smaller opportunities for those employed in Slovenia.

[5] Jus Miran: Financiranje izvoza in zavarovanje izvoznih kreditov (Financing of Exports and Export Credit Insurance), Amalietti, Ljubljana, 1992

ity, poor management or other reasons under his control or in his sphere of control and, consequently, manifest in his bankruptcy, compulsory settlement or similar event having as a result partially or totally uncollectable debts.

On the contrary, non-commercial risks stem from events beyond the control of the debtor or insured person and have a negative effect on the insured party (supplier, bank, investor, etc.) doing business with a debtor abroad. There are numerous non-commercial risks, such as: war, civil unrest, expropriation, nationalisation, moratorium, prohibition of transfer, conversion, prohibition of imports or exports, natural catastrophe etc. These risks may be high for exporters, especially for those trading with developing countries or debtors in politically unstable countries. In situations such as, there is a real danger of a foreign country taking measures such as preventing imports or restricting foreign trade. Exports to a particular country or receiving payments from there may be prevented by trade sanctions, embargo, blockades and closure of borders. Payment problems are often related with balance-of-payments problems of the debtor country reflected in the prohibited conversion of domestic to foreign currency or prohibited transfer of payments abroad. All these circumstances show how an event beyond the debtor's control may affect his payment obligation. The debtor may be prepared and able to meet his obligations, but cannot execute the payment because he has no influence on the events preventing meeting of obligations. This may happen even if the debtor is a large international corporation.

Insurance of the above-mentioned non-marketable risks in Slovenia is provided by the Slovene Export Corporation, an authorised institution according to the ZZFMGP. Elsewhere in the world and also in the European Union, state-support insurance is usually provided by one institution or through its affiliated persons. Institutions providing non-marketable insurance must comply with the WTO, OECD, EU and BU rules on insuring export credits. The business of Slovene Export Corporation already complies with these rules and therefore, no marked changes are expected upon accession to the EU. By the definition of non-marketable risks alone, no changes in competition in this area are expected, as foreign countries with their financial capacities have no interest in encouraging international expansion of the Slovenian economy. The Republic of Slovenia thus remains the sole provider of non-marketable insurance to Slovenian companies through an institution authorised by law. However, the status of state support changes in line with the previously mentioned regulation. In particular in the area of short-term trade insurance (credit terms of up to 2 years), the existing trends and increasing services provided by reinsurance companies indicate that state support is becoming less and less important, which is also in line with the Communication of the European Commission 2001/C 217/02, OJ C 217 as of 2.8.2001.

In the area of non-marketable risks, we can therefore not expect any direct competition from Export Credit Agencies of the EU Member States. However, competition will exist in the development and quality of products and services of Export Credit Agencies related to supporting the domestic economy in doing business abroad. The services which Slovene Export Corporation has developed in the 12 years of its existence are in general comparable with the services of foreign and established Export Credit Agencies, which not only enables Slovenian exporters to be more competitive on foreign markets but also allows Slovene Export Corporation to enter into agreements on co-insurance and reinsurance with similar institutions with the purpose of collaboration of the two countries in common projects.

ZZFMGP adopted at the end of 2003 has thus laid the grounds for insurance against non-marketable risks, fully comparable with systems in other countries and with Export Credit Agencies. Only the future will show whether we will be able to witness further positive development as recorded since 1992 or the development trend will – due to EU accession (which, however, according to the experience of other EU Member States should not negatively affect non-marketable insurance) and a redefined role of the state in ZZFMGP – slow down.

Conclusion

What is the future of credit insurance? On the basis of the business results of the members of credit insurance associations, it can be concluded that credit insurance has preserved the function of supporting national economic development despite the stagnation of the economy in the past years and somewhat poorer results of specialised credit insurance companies (which, however, already improved in 2003). On the contrary, numerous bankruptcy cases in the world in the past few years have spurred the demand for this type of insurance and the same can be said for the Slovenian domestic and export credit insurance market. In Slovenia, this insurance segment cannot expect to record the same level of growth as was recorded in the period from 1996-2001 as a result of already relatively high market penetration (compared to EU Member States). Nevertheless, in view of the interest of clients in the accompanying services, stable growth can be expected. Competition of credit insurance companies in the EU will affect business results but at the same time, the enlarged market will also bring about new expansion opportunities[6]. Given the specific features of trade credit insurance, certain caution will be needed however in doing business with clients from other countries who fail to obtain insurance with their local insurance companies due to various reasons (risky business, inappropriate internal risk management, poor results in the past, failure to pay premiums, etc.). Opportunities will, however, also increase by accompanying Slovenian export companies through affiliated companies in foreign markets and perhaps in the border regions. On

[6] Before expanding to foreign markets (as well as neighbouring markets) certain preparations are required, such as getting to know the specific features of these markets and the behaviour of clients in a different legal environment (despite the »EU«), adjustment of insurance terms and conditions, preparation of documentation in a local language, additional training of staff. Only partial entering of the EU market would thus not be rational and profitable.

the other hand, these opportunities will be lost if the ownership structure of the sole large supplier of this kind of insurance in Slovenia (Slovene Export Corporation or its future subsidiary insurance company) changes and if one of the largest European credit insurance companies with many local units in the EU market acquires a majority share. Regardless of the ownership structure, further development of this type of insurance as well as increased supply of services (e.g. fidelity insurance) may be expected in Slovenia.

Contrary to trade (marketable) credit insurance, no marked changes are expected upon Slovenia's accession to the EU in the area of consumer credit insurance, at least not until these are provided only by multi-line insurance companies. In the area of non-marketable insurance, the Slovenian government will preserve its leading role, which with its policy pursued under international regulations and conditions, provides support to Slovenian exporters.

The *crystal ball* being so popular among credit insurers, we will conclude with it as well. No single meeting of credit insurers has passed without it being mentioned at least a dozen times. It speaks of the unpredictability of this type of insurance, indirect influence of events which cannot be foreseen in advance. But it also speaks of the special attraction of this insurance, which was experienced only by persons engaged in this business and in risk assessment for a long period of time. Although having no crystal ball, they posses the necessary skills to judge the circumstances (as well as a feeling), which can substitute for insight into an unpredictable future. Together with all the instruments and mechanisms of risk assessment, this provides a future for credit insurers and preserves their somewhat unique status.

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