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Ad Hoc Expert Meeting on Insurance Services
Geneva, 24 November 2005

REPORT OF THE AD HOC EXPERT MEETING ON INSURANCE SERVICES

Held at the Palais des Nations, Geneva,

24 November 2005

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Chapter I

CHAIRPERSON'S SUMMARY

1. The Ad Hoc Expert Meeting on Trade and Development Aspects of Insurance Services and Regulatory Frameworks was held on 24 November 2005, convened by UNCTAD's Division on International Trade in Goods and Services, and Commodities (DITC). Insurance experts from Governments, regulators, trade negotiators, and representatives of the private sector, international organizations and civil society were invited to put forward their views on how to ensure development gains from the insurance services sector. There was a particular focus on how Governments of developed and developing countries could play an active role, at the national level and in multilateral negotiations, in maximizing benefits from trade in insurance services.

2. The UNCTAD secretariat had prepared a background note entitled "Trade and development aspects of insurance services and regulatory frameworks" (UNCTAD/DITC/TNCD/2005/15), which was commended as an important contribution. It was considered a good basis for the discussions as well as a source of input into the policy formulation process at the domestic, regional and multilateral levels. Also, participants welcomed the two case studies commissioned by the UNCTAD secretariat, which focused on the trade, regulatory and development concerns of the African and Chinese insurance markets.

3. Different views were exchanged and opinions expressed on the issues raised in the background note, in the two case studies and in the presentations made by the invited experts. The following text aims to reflect the richness and diversity of the views expressed and suggestions made during the meeting. The agenda and the attendance list are annexed to this report.

I. Insurance services and development

The multifaceted role of the insurance services sector

4. *Insurance services form part of the integrated world of global finance. They play a crucial infrastructural and commercial role in a country's economy.* From an infrastructural perspective the provision of insurance services is closely linked to macroeconomic factors such as inflation, national economic policies and the achievement of national development objectives. This is particularly important in the light of the fact that a well-functioning insurance sector promotes financial stability. As an infrastructural service, insurance services not only have the capacity to mobilize and channel savings (for example, life insurance companies effectively mobilize savings from the household sector and channel them to the corporate and public sectors) but can also support trade, commerce and entrepreneurial activities in other sectors. They do so, inter alia, by reducing the total risk faced by the economy. At an individual level the insurance sector can improve the quality of life of individuals and increase social stability. Insurance services can thus relieve the pressure on Governments' budgets. Strengthening the insurance sector can lead to the development of domestic capital markets, particularly in terms of long-term financing of government bonds. Also, corporate sector financing may be facilitated, for example through the reinvestment of insurance funds.

Global market trends in insurance services

5. The world insurance premium for 2004 stood at $3.244 trillion. Although nearly 85 per cent of the world's population is to be found in developing countries (also referred to as emerging markets), the global insurance market is dominated by industrialized countries, which account for 88 per cent of the global life insurance market and 90 per cent of the global non-life insurance market. However, *emerging markets are experiencing a rapid overall growth rate* (7.5 per cent for emerging markets as opposed to 1.7 per cent for industrialized countries), which indicates the significant potential for future expansion. Current growth rates are particularly high in Asia (e.g. China, which has a growth rate of 27 per cent adjusted for inflation). Also, insurance markets differ between developing countries, including in their growth rates and in their size. This is due to, among other things, variations in culture, insurance regulation and GDP.

6. *A number of market drivers have been highlighted in respect of insurance services.* (i) *Demand for insurance services.* Demand is determined by changes in demographics and wealth profiles, as well as cultural consumption and spending patterns. It will also be affected by the largely untapped emerging market in the East and the unutilized — or underutilized — saving capacities of people in the developed countries. (ii) *Regulation.* The past decade has seen increasing globalization and the opening up of financial services markets. It has also seen several failures, including the failures of insurance companies, both in developed and in developing countries. This has generated a need for corporate governance requirements and transparency, as well as careful regulation of the insurance sector. This is particularly important since failures in the financial sector can be very costly, potentially shattering the underpinnings of a country's economy and resulting in financial instability. With Governments striving to put comprehensive regulatory systems in place, some fear that this will result in a regulatory avalanche, which in turn would entail additional costs in implementation and compliance. (iii) *Increased liberalization and privatization of insurance services.* Increasing liberalization and privatization have occurred either independently or as a result of bilateral/multilateral arrangements. The bigger players in the global insurance markets have a crucial interest in continued liberalization, particularly in the context of the larger insurance markets, including China, South Africa, Brazil and India.

7. *The insurance sector is also subject to operational drivers,* and participants discussed, among others, the following: distribution; risk management and liability management; offshoring, outsourcing and operational capacity; and consolidation and economies of scale. (i) *Distribution.* It was noted, that except in Europe, distribution networks for insurance services are not as well developed as distribution networks for banking services. This is particularly true with regard to developing countries. Since the distribution of insurance services is less developed and more difficult to manage than the distribution of banking services, insurance services providers are forging alliances with banks to distribute their insurance products. This is part of a broader trend in terms of closer ties between insurers and banks, and has given rise to questions about the nature of regulation not only within the insurance services sector but also across the financial services sector as such. (ii) *Risk management and liability management.* The management of risk and liabilities is also undergoing changes, including trends towards pooling data and using modern, high-tech IT services. (iii) *Offshoring, outsourcing and operational capacity.* As in other sectors, there is a growing trend in the insurance services sector towards outsourcing certain services, inter alia for the purpose of improving cost-effectiveness. (iv) *Consolidation and*

economies of scale. There will continue to be a convergence of trends (in terms of size of markets and operations), building on an existing trend, towards the concept of "big will increasingly be beautiful". This applies to both the developing and the developed world.

8. Other trends include the increasing use of technology and the Internet, and the increasing disaggregation of insurance services that are provided. Attention was drawn to the fact that the latter would allow developing countries to capture specific, disaggregated processes as areas with export potential. Other key factors which can facilitate the integration of developing countries into the global insurance marketplace include development by domestic insurance suppliers of the expertise necessary for successfully engaging in the international market (essentially by building human capital and know-how), and development of micro insurance.

Insurances services in developing countries: Some characteristics and challenges

9. *Insurance markets in developing countries have a number of particular features.* These include their small size, undercapitalization, and institutions that are underdeveloped or do not exist, as well as insufficient experience and know-how. In many developing countries, insurance services are not yet considered a key component of the financial services sector. This results in a low profile, a lack of interest and the Government's allocation of insufficient resources to the development of the insurance sector. Divergences remain, both between developing countries and within the insurance market itself (for example, the life insurance sector, which could have the most widespread positive welfare impact, remains less developed, particularly in comparison with the non-life sector). However, more recently the size of developing countries' insurance markets has been growing substantially (despite a temporary fall in profitability in 2001–2002).

10. Nevertheless, developing countries face a series of specific challenges. These derive from, among others, the important infrastructural role of insurance services, the rapid evolution of the global financial and insurance markets, and the trend towards liberalization in the insurance services sector, as well as from the lack of human capital and skilled personnel.

11. *The first of these challenges relates to the importance of developing national strategies and policies, with due account being taken of national development objectives. This applies to both the financial services sector in general and the insurance services sector in particular.* The discussion emphasized the importance of developing a coherent strategy, particularly since in many developing countries the insurance sector is not yet considered a key component of the financial architecture. This has led to a lack of public awareness of the benefits and uses of insurance products, a lack of demand for such products, and ultimately an inadequately and scarcely diversified insurance sector. It was suggested that a broader, pro-development strategy for the insurance sector could start with a comprehensive and sound cost-benefit analysis of the insurance sector in individual countries (looking at, among things, existing financial service suppliers, demand for insurance products, institutional mechanisms, and so forth). This stocktaking could form a solid basis for setting out recommendations and future directions, and policies in line with national objectives. Such an exercise should focus on, inter alia, issues related to risk and how to avoid crises.

12. *The second of these challenges relates to the importance of setting up effective regulatory, supervisory and legislative structures as a prerequisite for liberalization.* Developing

countries face the challenge of preserving the integrity and viability of the financial infrastructure through effective supervisory and regulatory frameworks. These frameworks are even more important in the light of technological developments, new and hybrid insurance products (e.g. banc-assurance) and the liberalization and privatization of insurance services. However, frameworks in developing countries tend to be inadequate or, in some cases, are non-existent. Even when new legislation and structures are put in place, they may not be effectively implemented and old practices may continue to exist. It was pointed out that often this may lead to the continuing existence of weak insurers within the insurance market. Also, there are differences between the regulatory frameworks of developing countries and huge gaps between the frameworks of developing and developed countries. These differences make efforts to standardize regulation at the international level a difficult task.

13. *A third area of concern for developing countries relates to challenges with regard to liberalizing insurance services and admitting foreign players into the domestic market.* While, traditionally, the State has played a key role in the provision of insurance services, increasing diversification and differentiation of insurance-related consumer products have provided an increasing role for the private sector (especially institutions with diversified investment strategies). This has been intensified by the growing inadequacy of tax revenues to match the pension needs of an ageing population, particularly in developed countries.

14. Some participants believed that opening up might lead to increased competition, which could be favourable since it forces insurers to become more efficient and cost-effective. Other stressed that it was equally important that such competition take place on a level playing field. In sum, opening up brings benefits and challenges. On the one hand, the admission of foreign insurance companies can be beneficial in that it contributes substantial financial strength; transfer of technical, managerial and technological knowledge; global market credibility; and risk and asset liability management. On the other hand, the operation of foreign insurance companies can lead to anti-competitive practices; selective marketing to high-value clients; potential employment losses; and the need to carefully manage any balance-of-payments difficulties that arise.

15. One of the key issues as regards FDI in the insurance sector relates to the nature of the FDI regime. Some suggested approaches relate to the following: regulatory transparency (and the equal application of regulations); adherence to IAIS (International Association of Insurance Supervisors) standards; protection of FDI; freedom to invest (within prudential limits), including by allowing realistic foreign capital levels and not requiring uneconomic cross-subsidization; and freedom to reinsure if necessary in global reinsurance.

16. *A fourth area which was considered to pose a challenge for developing countries related to the need to overcome supply-side constraints and promote the operations of domestic insurance suppliers and nascent industries.* It was stressed that this is an area where the Government can and should play an important role.

17. In essence, the specific supply-side constraints which developing countries face are a lack of diversified insurance products within their insurance markets. This weakness derives from, inter alia, a weak supervisory and regulatory environment, a lack of sufficiently well developed distribution networks, and, more broadly, a lack of public awareness about insurance products

and their usefulness (often linked to social and cultural aspects in terms of attitudes towards risk, which has resulted in constraints on the demand side). Also, infrastructure constraints play a major role; in fact, there is, inter alia, a lack of technical skills, particularly human skills; a lack of well-developed institutional mechanisms (e.g. for information and data collection); and insufficient use of information technology (e.g. as a tool to facilitate insurance operations and risk assessment). *There is, therefore, a need to strengthen the regulatory environment so as to include appropriate legislation, taxation policies and effective enforcement mechanisms, as well as to effectively build human capital.* Using auxiliaries and intermediaries (e.g. agents and brokers) could also help raising public awareness and facilitate distribution.

A closer look at Africa: The example of the life insurance sector

18. The meeting dealt in depth with the functioning of, and the difficulties faced by, African insurance markets, with a particular focus on the life insurance industry. *Overall, the African continent has varying levels of development. The African insurance market is dominated by South Africa, which generates 79 per cent of the continent's premiums.* While Africa has taken the lead in several areas (e.g. in catastrophe insurance and by setting up the African Insurance Organization), much remains to be done.

19. Discussants drew attention to what could be among the most things to do in that context: training the trainers (including training at the level of government officials) and creating facilities for insurance professionals and regulators to network and specialize in core areas of insurance education. Also, studying what is needed to build both regulatory and market capacity would prove useful. Another important challenge is the setting up of stringent regulatory and supervisory standards (on a par with international standards and meeting obligations under the WTO); the provision of insurance services to the rural and agricultural sector and the urban informal sector; and the development of a strategy for catastrophe risks as well as an enabling environment for life and pensions. Since any move towards addressing these challenges would involve substantial outlays (in financial, human and technical terms), African countries would benefit from external assistance.

20. The meeting also focused on the African life insurance sector. Life insurance is important (particularly for developing countries) because of its ability to mobilize and channel savings. In Africa, the life insurance industry is characterized by regional peculiarities. The South African life insurance industry is highly developed and has always been in the forefront of life insurance. In fact, some of the first linked investment products (e.g. insurance products where a specified part of the premium is invested in securities and funds) originated in South Africa. In comparison, the life insurance sector in anglophone East and Southern Africa is significantly underdeveloped. In some of these countries, the majority of the business relates to pension investment, coupled with group life risk cover. The anglophone/West Africa market consists of six to seven countries, with Nigeria being the largest insurance market. The Nigerian market (over $50 million) comprises around 100 insurers licensed to write life business. Changes in Nigeria's legislation will give rise to significantly higher capital requirements in the near future. This is expected to result in mergers and acquisitions and the issuance of fewer life licences. It is estimated that if the capital of all existing life licences in Nigeria were combined, there would be enough capital to set up about three companies under the new regime.

21. Francophone Africa comprises 16 countries, of which 12 participate in the CIMA insurance code (Conférence interafricaine des marchés d’assurance, Inter-African Conference on Insurance Markets). There are approximately 60 insurance companies licensed to do business in one or more of those countries. Life insurance in this region is fairly simple by European standards and is almost all term insurance or very simple investment business (running on an accumulation basis). In comparison with other regions, the life insurance sector in the francophone region has a number of positive features, including strong local reinsurance support, adherence to the CIMA code (which has brought much-needed standardization) and, compared with anglophone areas, better training facilities and more readily available data.

22. *Despite regional differences, it is possible to identify certain common areas of challenge for the African life insurance industry.* Experts pointed out that one of the more *serious challenges relates to the AIDS epidemic and its negative impacts on average life expectancy.* They explained that some insurance companies have successfully modified their strategies in response to the AIDS risk factor. For example, companies sell what is termed funeral insurance (an approach being described in relation to AIDS coverage in South Africa), with higher, annually reviewed rates (when compared with normal term assurance rates); the use of universal life products allows insurance companies to change mortality charges without changing overall premium rates; and there is periodic (every five years) HIV testing (in the South African case, premium rates for policyholders who do not undergo (or fail) the tests increase significantly), and innovative use of an increasing term insurance in order to combat the AIDS risk (as undertaken by a Malawi life insurance company).

23. Experts also identified another *common challenge, namely the lack of good administrative systems and central statistics*. Only a few (usually the more profitable) companies use reliable systems, while others conduct their business on spreadsheets, use unreliable in-house systems or use manual administration. As a result, losses may be identified when it is too late to take remedial action. A third common challenge relates to the existence of insufficient and often archaic regulatory framework and solvency margins. A good example is the use of the United Kingdom's Insurance Act dating from the 1940s in many parts of anglophone East and Southern Africa. However, countries such as Namibia, South Africa, Mauritius, Ghana and the United Republic of Tanzania have taken the initiative and are currently redrafting their insurance legislation.

24. *Other challenges in the life insurance industry relate to a high number of withdrawals; low life expectancy; negative perceptions regarding the industry; lack of management experience and insurance skills; and the lack of transparency of charges on savings-type products.* In terms of solvency margins, a risk-based capital approach is rarely followed and the solvency requirements are, in some cases, meaningless. Experts also referred to the problem of giving insufficient consideration to the investment matching of liabilities, a problem which often stems from the absence of appropriate investment avenues (e.g. in the case of life insurance, where sufficiently long-term government bonds would be a valuable investment avenue).

25. It was pointed out that *despite all the problems Africa is facing, it is still possible to run a successful life insurance operation in almost any country in Africa.* This could be achieved by ensuring that adequate solvency regulation is put in place; by making available meaningful (and credible) assured life statistics (particularly assured life mortality tables by region); by creating

new and relevant products; and by training insurance staff, updating legislation and providing incentives to the industry.

The multiple roles of the Government: Regulator, facilitator and provider of insurance services with a view to enhancing development

26. The role of the Government is not confined to that of regulator and supervisor of insurance services. Rather, as experts pointed out, the *Government plays a very important role as a facilitator, including by ensuring access to insurance services as well as overcoming obstacles in the development of the insurance services sector.* This is done by coordinating and setting out a financial services policy with national development objectives in mind, creating an enabling environment through appropriate legislation, ensuring cooperation among all stakeholders and policymakers (industry, insurers, consumers, tax authorities, judicial authorities) and, more broadly, ensuring effective engagement at the multilateral level both at the WTO and in international standard-setting processes. Other examples of government engagement include the establishment of public–private partnerships, for example in the area of data exchange, management and reporting systems.

27. Two particular questions arose as regards the Government's role as a provider of insurance services. The first related to the importance and nature of the role that Governments play; and the second related to how the Government would finance its provision of insurance services. As regards the first question, there are types of insurances which would benefit lower-income and rural sections of the population. These include agricultural insurance, catastrophe insurance and micro insurance, as well as social security schemes. In that context, it is important to remember that very often the supply of such insurance services to lower-income segments of the population is considered non-profitable by private insurance suppliers. Thus, in developing countries, the Government should play an important role in ensuring that insurance services are accessible to large lower-income segments and the rural sections of the population.

28. Thus, as suggested, in the interest of providing a public good, the Government may choose to act as a provider of insurance services to these sections or to create an enabling environment for other insurance service suppliers to operate in. This could be done by putting in place support mechanisms (e.g. assistance with risk assessment, data collection); acting as a reinsurer; creating public awareness; setting up favourable regulatory and enforcement mechanisms; and allowing the use of existing distribution networks such as banks and post offices for the distribution of insurance products or exploring alternative insurance schemes (e.g. community-based schemes for rural populations or bank account holders receiving insurance instead of interest, mechanisms for strengthening rural insurance or micro insurance). One expert pointed out that the Government should not act as a primary insurance supplier but rather as a facilitator. Catastrophe insurance is another area of concern for developing countries, given the extent and widespread nature of damage. The Government can act as a reinsurer in this sector since insurance companies may be willing to cover only a part of the risk arising. In 2004, the African Insurance Organization set up the Catastrophe Insurance Centre in Morocco, the objective of which is to collect information, map risks, and provide comprehensive services, contacts and information in relation to catastrophes (including an annual report) for all Governments in Africa and for the relevant agencies.

29. While the Government can and should play a role as an insurance service supplier or facilitator in the provision of insurance services, it is important that this role be played with due account being taken of the financial bottom line in the provision of such services.

II. Insurance services and the emergence of new regulatory frameworks: Challenges for developing countries

Insurance services and international regulatory standards

30. *By setting out clear rules of the game, international standards and harmonization can help improve the functioning of the markets, and perform an important guiding function for domestic reform processes*. Regulators in both developed and developing countries are faced with newer regulatory challenges arising from the increasingly heterogeneous and complex nature of the insurance sector, challenges from technological developments and those from the new and hybrid insurance products, as well as the shifting focus of regulation. For developing countries whose regulatory frameworks are minimal or in the process of being developed, these problems create particular challenges.

31. In this context, the IAIS (International Association of Insurance Supervisors) is mandated not only to set international standards, but also to help member States to implement those standards. By focusing on core principles, IAIS standards tend to be simple and clear. Some noted that this would avoid overregulation or the creation of a "regulatory avalanche". Frequently, these standards serve as mere "guiding principles", allowing regulators to fit any implementation to their country's particular developmental needs. Specific other country experiences can help shed light on how to manage such regulatory transition processes.

32. Guatemala, for example, is in the process of revising current insurance laws, many of which date back to the 1950s and 1960s. While a reasonable amount of Guatemala's law reform process is based on IAIS standards, the country is also conscious of the limits of international standards, notably the need to adapt regulatory standards which suit its particular developmental needs. In this regard, the IAIS principles are considered to be guiding principles, which, as they have a degree of flexibility, can be adapted as necessary. Also, it was pointed out that regulation can be extremely burdensome for companies. Finally, regulatory challenges for developing countries are not always a North/South issue: they can frequently arise from the need to properly differentiate between small and medium-sized enterprises and transnational companies.

33. Despite such positive experience, overall, *developing countries still face difficulties in terms of complying with IAIS standards,* one of the reasons being that regulators receive only limited support from Governments. This is compounded by the problem of keeping up with the rapid developments in the markets. There is therefore a need for assistance, cooperation and expertise, including for the purpose of improving data and monitoring market developments.

34. *International standards can also play a key role in relation to the liberalization of insurance services, including in the WTO framework.* There is the challenge of realizing (and responding appropriately to) the differences between liberalizing trade in goods and trade in services. It was pointed out that adopting common standards can be an important first step to

overcoming difficulties related to liberalization. An example of that is the case of Europe, where common standards helped to achieve liberalization.

35. While compliance with international standards can help countries improve their reputation and facilitate synergies with the global insurance market (thereby helping developing countries, particularly those in Africa, to benefit from globalization), experts also pointed to the need for an examination of domestic regulatory frameworks and structures, and for identification of how developing countries may benefit from international standard setting, as well as to the implications of international standard setting and to developments in insurance liberalization at the multilateral level. UNCTAD was commended for having provided valuable inputs and was asked to step up its efforts in this context. This would include capacity building (e.g. as part of the agenda in economic recovery programmes under the World Bank and the International Monetary Fund) and improving Governments' support for regulators in the insurance sector. In that connection, it was suggested that Africa develop a common strategy as regards liberalization of insurance services in the WTO.

Africa's emerging regulatory frameworks and international standards

36. Africa provides an interesting example of the challenges that developing countries face in the context of liberalizing insurance services. As regards international standards, there is a wide gap in terms of knowledge between regulators in developed markets and those in Africa. Nevertheless, it is estimated that nearly 80 per cent of supervisors have adopted some sort of international regulatory standards. Within Africa, most of the insurance regulatory bodies (except those in South Africa) are experiencing problems. Most of these *difficulties relate to the shortage of techniques for risk analyses and measurements, the need for regulators to be autonomous, and the lack of clear goals and strategies, as well as an overall low level of insurance awareness, which results in a low level of insurance penetration.* Other challenges stem from the fact that Africa is mainly a non-life insurance market, and that the insurance industry has not been perceived as being innovative enough to offer services of interest to the everyday consumer.

37. Thus, except in South Africa, insurance practice in Africa has yet to catch up with the global developments in regulatory infrastructure. Despite obvious challenges, harmonization and international standards can help in this process. According to some participants, experiences suggest that Africa can indeed achieve a certain degree of harmonization (despite important cultural and political divisions). The successful experience of the East African Community with motor, fire and property risk insurance is a case in point.

38. The African Insurance Organization (AIO) is another example of a regional initiative. The AIO constitutes a joint effort to improve risk management in African countries. Its objectives are to gather information and data and make them available to African countries, to create a network for that purpose, and in that context to tap the potential and expertise of companies, insurance brokers and relevant entities from abroad. Participants commended the AIO for taking the initiative in facing challenges and limitations, and highlighted the need for further funding to continue that endeavour, including through support by UNCTAD.

China's emerging regulatory framework and its WTO accession

39. *China provides an interesting and positive example of the liberalization and regulation of insurance services.* In fact, a closer look at China *reveals the linkages between its domestic reform process and its accession to the WTO*. In 1998 the Chinese Insurance Regulatory Commission (CIRC) took over from the People's Bank of China as the main regulator of the insurance sector. The CIRC works according to the "1 plus 3 principle", whereby the Central bank collaborates with three government agencies, which focus respectively on banking, securities and insurance. The establishment of the CIRC has greatly strengthened the supervision of the insurance industry.

40. China's accession to the WTO prompted the establishment of a series of new legal frameworks, including as regards so-called foreign funded insurance companies, insurance agents, brokers and reinsurance. In pursuing its regulatory objectives, the CIRC covers a broad array of issues and uses a series of regulatory tools. The latter include the following: *the regulation of market entry*, where the CIRC has loosened formerly strict limitations on market access and areas of operation (this has led to an increase in the number of foreign insurance companies); *the regulation of clauses and premium rates*, where despite a loosening of formerly strict limitations on clauses and premium rates, insurers are still required to obtain prior approval for certain insurance products (e.g. mandatory insurance products, products recognized as being in the public interest and life insurance carrying death protection); *the regulation of insurance investment*, where a 1995 law placed strict requirements on insurance investments (with the goal of ensuring the solvency of the insurance companies); *the regulation of market behaviour* (regarding sales, marketing, insurance agents, advertisement, policy dividends, investment returns, misrepresentation, biased comparison between products etc.); and *the regulation of insurance solvency*, which requires companies to ensure a certain, calculated solvency margin or the regulation of foreign-funded insurance companies.

41. More specifically, China's entry into the WTO prompted the promulgation of the Regulation on the Administration of Foreign-funded Insurance Companies, with a more detailed regulation following in 2004. The latter establishes the so-called 523 requirements, under which the applicant's total assets should be more than $5 billion at the end of the year before application; the applicant should have established its representative office(s) two years before applying; and the applicant should have had over 30 years of experience in the insurance business. While at first glance, these appear to be stringent requirements, it was noted that almost every foreign applicant meets the criteria. Another focus of the CIRC is risk prevention, which is approached on the basis of five lines of defence: (i) enforcing the internal control of insurance companies; (ii) enforcing the regulation of solvency; (iii) reinforcing on-the-spot inspections; (iv) enforcing the regulation of insurance investments; and (v) establishing and completing the system of insurance protection.

III. Insurance services in the GATS and the interests of developing countries

Insurance services commitments and offers submitted to date

42. *Financial services — and insurance services as part of them — are the second most committed sector after tourism.* Overall, the insurance services commitments that WTO Members have entered into are *skewed in favour of Mode 3 as opposed to Modes 1 and 2*. There are only a

few instances of full commitments. Thus many Members maintain limitations on the entry of insurance providers, with the most commonly found limitations being foreign equity limitations, followed by limitations related to restrictions on foreign branching. Other limitations relate to the type of legal entity and quotas on the number of suppliers, especially in reinsurance services.

43. *In the current round of negotiations, the offers submitted so far indicate that there has not been a substantial change in the overall picture/pattern of commitments*. Out of 69 offers, 30 contain some sort of improvements in relation to insurance services, either by including new subsectors or by making improvements to existing commitments. One expert pointed out that, in general, offers are minimal and fall short of what could be achieved (i.e. considering what the current national-level practice already allows). It was also pointed out that during the Uruguay Round, developed countries made relatively deeper commitments (especially on Mode 3). Also accession countries have made deep commitments. In the current round of negotiations further and deeper commitments have been sought specifically in cross-border trade in insurance services.

44. Proposals submitted during the current negotiations relate to the elimination of barriers to establishment, the right to establish any type of legal form and the elimination of discriminatory limitations. Some of the most extensive proposals even address regulatory issues, most importantly the need to interpret the scope of the prudential carve-out contained in the annex on financial services. Several proposals also address transparency issues, including transparency specific to licensing and qualification requirements. It was pointed out that *the importance of regulatory reform was widely recognized and accepted as a prerequisite to liberalization* within the insurance services sector; this suggests that there is a need to ensure proper sequencing between liberalization and regulation.

45. As regards Modes 1 and 2, some proposals suggest liberalizing these modes and clarifying classification issues in that respect. In fact, technological and market developments have resulted in the blurring of distinctions between Modes 1 and 2. Clarity has also been sought about whether the annex on financial services or the UN CPC is the preferred method for the classification of insurance services and subsectors. Another area that has given rise to discussion is the scope of Article I 3 (b) of the GATS, which relates to "services supplied in the exercise of governmental authority". Regarding this provision and the annex on financial services, participants raised questions about their definition and scope.

Complementary/alternative approaches to liberalization

46. More recently, some Members have indicated their disappointment about the progress made so far in the services negotiations. In that context, they suggested *complementary approaches (including measuring and targeting) as a tool to meet quantitative and other qualitative objectives*. Suggestions for qualitative thresholds focused on the elimination of limitations, while suggestions for quantitative targeting focused on liberalizing a fixed percentage of subsectors within specified sectors. Developing countries would be permitted to have a lower percentage target to be met, while LDCs would not be required to make any changes. Another *alternative suggestion was using the plurilateral approach to negotiations*, whereby a group of countries interested in opening up specific sectors may come together and formulate liberalization proposals, with the outcome of the negotiations applying on an MFN basis. *Many*

developing countries have not been supportive of the newer approaches to the liberalization of services, as they could imply a loss of flexibility, have a negative impact on the architecture of the GATS, and raise questions as to the costs of autonomous liberalization and binding (where the issue of reciprocity comes in), as well as the extent and depth of the commitments that would be required.

47. Attention was drawn to another tool that would merit attention in this context, namely *the model schedule for future commitments in insurance services, as proposed by the Financial Leader's Working Group*. The objective of this schedule is to provide for equal treatment for insurers and *to address issues relating to effective market access for insurance providers* through the prescription of guidelines for scheduling liberalization commitments within the GATS framework. The model schedule consists of two parts, the first one relating to market access and national treatment commitments, and the second one taking the form of additional commitments, including on regulatory measures (the idea behind this part being that it would be uniformly adopted by a critical mass of Members). It was pointed out that the use of the model schedule has to factor in differences in the regulatory capacities of countries. Thus, while the model schedule affords greater predictability and comparability of commitments, the need for individual flexibility also has to be recognized. The need to further examine the template's development implication was pointed out.

Insurance services, GATS and the interests of developing countries

48. It is important for developing countries to ensure that current negotiations on the liberalization of services, including insurances services, deliver development benefits to them. *A comprehensive assessment can help developing countries to identify their interests in insurance trade negotiations, at both the multilateral and the bilateral levels.* Such an assessment would include a comprehensive examination of those areas where developing countries either have or can develop a comparative advantage, which can be developed into areas of export interest. Developing countries must also identify those areas which could benefit from some level of foreign private sector participation (e.g. areas where there is a need, but insufficient domestic capacity to meet this need). In any event, *liberalization within the insurance services sector specifically needs to take place gradually, with careful sequencing and pacing based on each country's development objectives.*

49. It was pointed out, in the Indian context, that the objective of trade policymaking in the insurance sector is closely linked to the achievement of sustainable development within the sector. The spin-off effects of this approach are to ensure that insurance services have a wider reach (particularly to the rural population) and that equity and regulatory capabilities are strengthened. In this regard, liberalization and reform should be concomitant, especially for insurance where the regulatory capabilities of countries are very different.

50. Despite the fact that the provision of insurance services is a capital-intensive activity, there are areas in which developing countries can develop an export interest, which in turn could be facilitated through GATS market opening. It was stressed that more broadly, developing countries can avail themselves of opportunities provided by the global trading system and the newer trends in the global insurance market. Experts and participants provided different ideas for areas where developing countries could develop an export interest, including outsourcing and

offshoring (e.g. Modes 2 and 3 trade); the provision of insurance services through Modes 3 and 4; the distribution of insurance services and insurance intermediation (particularly as targeted to the local level); leveraging advantages based on knowledge of local markets; developing software services related to the insurance sector; enhancing the portability of insurances (e.g. health insurance); and looking at possibilities for South–South cooperation and trade.

IV. The way forward: Policy conclusions and recommendations

51. As discussed in the Ad Hoc Expert Meeting, *the insurance sector presents a series of challenges and opportunities for development*. There is, therefore, a need to properly understand these challenges and to identify what could be done to assist developing countries in facing them.

52. To begin with, there is a need to recognize that *globalization may have different implications for developed and developing countries*. It was pointed out that shocks or developments that are marginal or gradual for industrialized countries may have far-reaching implications for developing countries. Examples include development challenges arising from the reversal of FDI, from weaknesses of particular insurers or from the increasing cross-sectoral linkages (e.g. between banks and insurers), it being noted, however, that the latter can also present challenges for developed countries. Broadly, globalization highlights challenges related to financial stability and the need to focus on macroeconomic aspects. However, there is not yet a clear recipe for the appropriate pacing and sequencing of reforms while liberalization (autonomously and at the national level) is proceeding. The recognition that liberalization alone is not enough may be one of the reasons for the hesitation of some countries in the context of the liberalization of insurance services.

53. Besides macroeconomic issues, long-term strategic challenges related to the liberalization of insurance services also exist in the need to build supply capacities, train insurance professionals, develop regulatory frameworks and raise public awareness. More broadly, many of these questions also come down to the nature of reforms, which can be either gradual or radical. So far, however, there is no clear evidence as to which of the two it is better to pursue. Some suggest that a gradual approach may avoid the most painful of the transition experiences and failures and generate more sequenced and carefully paced reforms of laws, regulations and insurance enterprises. At the same time, it was pointed out that gradual reforms run the risk of being captured by vested interest groups, a challenge which the WTO framework can help to address.

54. According to some experts, the WTO framework can also offer some more tactical opportunities, particularly arising from the current GATS negotiations. This is despite the GATS' legacy in terms of relatively limited liberalization effects flowing from past negotiations and the broad array of issues that need to be addressed (e.g. definitional issues or prudential regulation). Some, in fact, perceive current discussions on the plurilateral approach as offering advantages, both for negotiators (as this approach would be based on precedents, offer a certain degree of flexibility, enhance confidence and avoid blocking by those reluctant to engage etc.) and particularly for foreign investors (as plurilateral negotiations offer the prospect of resulting in similar liberalization commitments across countries, which in turn enhances transparency and predictability for investment).

55. While developing countries (e.g. those in Africa) may realize opportunities from the liberalization of insurance services (including WTO liberalization), many benefits may arise only in the long term. In the short term, however, there are challenges arising from significant adjustment costs, as well as other problems arising from the inability to capture benefits. Sub-Saharan Africa, for example, is not a major player in insurances services, including because of lack of technical capacities, knowledge and training.

56. *There is, therefore, a need to strengthen domestic and regional capacities so as to allow developing countries, their regulators and their insurance providers to play an effective role*. In this regard, it was pointed out that assistance from and cooperation with international organizations, including UNCTAD, can facilitate management of the regulatory and liberalization process, thereby enabling companies and regulators to perform better, and, ultimately, to better serve the interests of consumers. However, further funding and support are needed, including from donors and multilateral institutions, in order to continue developing these efforts, as well as supporting regional processes. There is an intention to work collectively to improve data, and there is a need for donor contributions in this context. UNCTAD has in the past collaborated with AIO, but there is a need for it to be further involved.

57. One key step for developing countries is *to have a strategic and clearly defined national policy on the financial services sector in general and on the insurance sector more specifically* (taking into account each country's specific national development objectives). This should be *accompanied by the development of efficient and effective regulatory and supervisory frameworks*, in line with international initiatives. In addition, there is a need to raise public awareness about the benefits of the insurance services sector and to invest substantially in building human capacity through the training of insurance professionals (for both the regulatory and the private sector, and as regards general insurance issues as well as specific sets of skills concerning risk management, accountancy and actuarial issues). Similarly, developing countries could strive to harness technological developments with a view to improving infrastructure (e.g. for information collection, regulation and data collection) for developing specific areas of export interest.

58. Also, the use of regional/South–South cooperation should be explored, for example in terms of pooling technical and financial resources and expanding insurance services trade. This was suggested in the Arab but also in the African (e.g. COMESA) context. Sub-Saharan Africa does not play a meaningful role in the world insurance market, and building regional capacity is therefore essential.

59. In all these aspects, the Government has multiple roles to play, ranging from regulator and facilitator to provider of insurance services. The challenge is to reconcile efficiency and social considerations, particularly for lower-income and marginal sections of the population.

V. UNCTAD's contribution and future work

60. With a view to achieving the Millennium Development Goals, and building on UNCTAD's longstanding work on insurance, UNCTAD could:

(a) Analyse the contribution of the insurance sector to economic and human development;

(b) Provide data and information on, for example, weaknesses/strengths, challenges or the presence of developing country enterprises in developed and developing countries:

(c) Facilitate the assessment of insurance services at the subsectoral level. This would assist developing countries, particularly LDCs, in formulating domestic policy options and in defining negotiating positions and strategies in multilateral, regional and bilateral trade negotiations;

(d) Analyse trade opportunities arising from the global trading system and evolving trends in the global insurance market as well as ways and means of facilitating such trade with a view to enhancing developing countries' exports. This could include an analysis of measures that Governments/regulators may put in place to maximize benefits and minimize challenges arising from international trade (and investment) in insurance services;

(e) Identify the regulatory challenges arising from the global/international nature of trade in insurance services, including in terms of cooperation, monitoring and enforcement, as well as possible responses at the national and international levels;

(f) Identify the impacts of liberalization, privatization and increasing investment in the insurance sector, as well as whether these impacts differ across countries and the trends and similarities arising from liberalization;

(g) Identify measures that Governments/regulators can take to improve domestic efficiency and to address supply capacity constraints in developing countries' insurance markets. Related to this would be an identification of the exact nature of the role of Governments, both as regulators and as providers of insurance services;

(h) Analyse the effects which economic and financial crises have on the growth of the insurance services sector (e.g. in terms of employment and economic development);

(i) Provide an understanding of the possible impacts that the consolidation and restructuring of financial sectors have on financial services trade (in terms of the extent to which reforms enhance competition and consumer welfare);

(j) Provide an understanding of the implications of technological innovations for the structure of financial services industries and markets:

(k) Look into the effects which the general trend towards the privatization of State-owned financial institutions has on the structures of financial industries and markets, as well as the regulatory challenges arising therefrom;

(l) Analyse the impact of the GATS and the ongoing negotiations to liberalize services trade (including negotiations on domestic regulation) and how they reflect current realities. Such an analysis could discuss the impact that current negotiations could have on the insurance sector, as well as the development challenges arising from recent suggestions about complementary and other approaches;

(m) Provide an understanding of the technical challenges that WTO Members face and the problems that may be encountered when interpreting the scope of the prudential carve-out as defined in the GATS Annex on Financial Services;

(n) Provide for key technical assistance and capacity building, satisfying the needs of developing countries in terms of assistance with international trade in insurance services;

(o) Conduct an analysis of the potential for and existence of South–South and regional co-operation (for example, as suggested in the Arab and African context);

(p) Assist in revising national legislation in line with international commitments, including through a model law on insurance legislation to provide guidelines for developing countries (for example, as suggested in the context of the United Republic of Tanzania).

Chapter II

ORGANIZATIONAL MATTERS

A. Convening of the Expert Meeting and agenda

61. The Ad Hoc Expert Meeting on Insurance Services was held at the Palais des Nations, Geneva, on 25 November 2005. H.E. Mr. Assad Omer (Afghanistan) chaired the meeting. The meeting had one agenda item, namely the substantive agenda item as set out in the programme in Annex I of this report.

B. Documentation

62. For its consideration of the substantive agenda item, the Ad Hoc Expert Meeting had before it a note by the UNCTAD secretariat entitled “Trade and development aspects of insurance services and regulatory frameworks” (UNCTAD/DITC/TNCD/2005/15).

63. At its closing meeting, the Ad Hoc Expert Meeting authorized the Chairperson to prepare the final report of the meeting under his own authority.

Annex I

PROGRAMME

10.00-10.30 **Opening Session**

- Mrs. Lakshmi Puri, Director, Division on International Trade and Commodities

- Mina Mashayekhi, Head, Trade Negotiations and Commercial Diplomacy Branch

10.30-11.30 **First Session: Global market trends in insurance services**

This session will provide a snapshot of the global insurance services sector in terms of volume, rate and sectors of growth, regional configuration and emerging trends within the market (including liberalization of insurance services and investment in emerging markets). The session will also touch upon the impact of liberalization and investment on insurance markets in Asia, Africa and Latin America, as well as private sector interests and what determines the private insurer's decision to invest in the insurance service sector in emerging markets.

Panellists followed by interactive debate

11.30-12.15 **Second Session: The role of insurance services in economic development**

This session will look at how to harness the insurance sector for development benefits. It will address measures that can be taken to improve domestic efficiency and address supply capacity constraints. It will look at urgent challenges and actions, both at the national and the international level, to safeguard a functional insurance market at the service of the national economy and encourage international trade. It will examine the impacts which the emergence and growth of the global insurance services sector can have on developing countries in terms of: the costs and benefits of insurance services liberalization; access to insurance products; risk management; enabling enterprises to cover risks efficiently; and mobilizing personal savings. Finally, the session will further address the question as to the role the government can play as a provider of insurance services as a public good.

Panellists followed by interactive debate

12.15-13.00 **Third Session: Insurance services, regulatory frameworks and international regulatory standards**

This session will consider whether the regulatory frameworks in developing countries are prepared for integration into the global insurance markets. In this context it will specifically address: (i) the importance of a strong national regulatory framework and its essential elements; (ii) harmonization of regulations regionally and internationally, and the implications thereof on developing countries; and (iii) whether there is a need for more active involvement, including because of the potential nexus between GATS and international standards.

Panellists followed by interactive debate

15.00-16.00 **Fourth Session: Liberalization of insurance services in the GATS and developing countries: The way forward**

This session will examine the state of play of GATS negotiations in the run-up to the WTO Hong Kong Ministerial, focusing on their relevance for the insurance sector. More specifically, the session will discuss:

(i) The assessment of the initial and revised offers and proposals for insurance services;
(ii) The impact that proposals for complementary approaches or model schedules can have on developing countries;
(iii) Ways and means of implementing Articles IV and XIX (2) in the context of insurance services;
(iv) Whether developing countries have the regulatory and financial service infrastructure needed;
(v) Potential areas of export interest to developing countries.

Panellists followed by interactive debate

16.00-17.30 **Fifth Session: Globalization and insurance: The challenges ahead for developing countries**

This session will aim to sum up the challenges and opportunities for developing countries from a regulatory and trade negotiations perspective. It will give pointers for building supply side capacity, as well as identifying areas of export potential for developing countries. What actions need to be taken, and by whom, to assist developing countries to harness the developmental benefits of the insurance sector?

Panellists followed by interactive debate

17.30-18.00 **Closing: Summary of discussions; the way forward**

Annex II

ATTENDANCE

1. Experts from the following member States of UNCTAD attended the Meeting:

Algeria
Azerbaijan
Belarus
Benin
Burundi
Cambodia
China
Egypt
Ethiopia
Eritrea
Ghana
Guatemala
India
Indonesia
Japan
Jordan
Morocco
Mozambique
Nigeria
Pakistan
Poland
Republic of Korea
Russian Federation
South Africa
Syrian Arab Republic
Sweden
Switzerland
Tunisia
Turkey
Ukraine
United Kingdom
United Republic of Tanzania
Zimbabwe

2. The following intergovernmental organizations were represented at the Meeting:

European Commission
International Monetary Fund
World Trade Organization
International Association of Insurance Supervisors
United Nations, New York, Department of Economic and Social Affairs
Common Market for Eastern and Southern Africa

3. The following non-governmental organization was represented at the Meeting:

International Confederation of Free Trade Unions

4. Representatives from the following organizations also attended the meeting:

German Insurance Association
Financial Sector Reform and Strengthening (FIRST) Initiative

5. The following panellists addressed the Meeting:

Global market trends in insurance services

Mr. Chris Gentle, Director, Global Financial Services Industry Research, Deloitte Touche Tohmatsu
Mr. John Cooke, Chairman, Financial Leaders Working Group, Insurance Team
Mr. Basil Reekie, Chief Executive Officer, QED and Chairman, African Life Committee
Ms. Patrizia Baur, Senior Economist, Swiss Reinsurance Company

The role of insurance services in economic development

Mr. Yoseph Aseffa, Former Secretary-General, African Insurance Organization
Mr. Nigel Easton, Head, UNCTAD Insurance Industries Programme
Mr. Udaibir S. Das, Division Chief, Exchange Regime and Debt and Reserve Management Division, Monetary and Financial Systems Department, IMF

Insurance services, regulatory frameworks and international regulatory standards

Mr. Yoshihiro Kawai, Secretary General, International Association of Insurance Supervisors
Mr. Wei Zheng, Secretary General, China Center for Insurance and Social Security Research
Mr. Israel Kamuzora, Commissioner of Insurance, United Republic of Tanzania, Member, Executive Committee, Association of African Insurance Supervisory Authorities

Liberalization of insurance services in the GATS and developing countries: The way forward

Mr. Juan Marchetti, Counsellor, WTO Trade in Services Division, Secretary of the WTO Committee on Trade in Financial Services
Mr. Jürgen Huppenbauer, European Committee of Insurance
Mr. Sumantha Chaudhuri, India

Globalization and insurance: The challenges ahead for developing countries

Mr. Yoseph Aseffa, Former Secretary-General, African Insurance Organization
Mr. John Cooke, Chairman, Financial Leaders Working Group
Mr. Wei Zheng, Secretary General, China Center for Insurance and Social Security Research
Mr. Ahmed Zinoun, Executive Manager, Société Centrale de Réassurance (SCR), Casablanca, Morocco
Mr. Udaibir Das, Division Chief, Exchange Regime and Debt and Reserve Management Division, Monetary and Financial Systems Department, IMF

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