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**PROBLEMATIC ASPECTS AND TRENDS OF REFORMATION OF
INSURANCE MARKET STATE REGULATION IN UKRAINE**

The main problematic trends of state regulation of insurance activity in Ukraine are investigated in the article, their negative impact on the formation of an effective and valuable national insurance market is revealed. The priorities for reforming of state regulation of the insurance market of Ukraine are outlined.

Keywords: insurance market, government regulation, insurance activities, reinsurance, tax, integration.

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**ПРОБЛЕМНІ ТЕНДЕНЦІЇ ТА НАПРЯМКИ РЕФОРМУВАННЯ
ДЕРЖАВНОГО РЕГУЛЮВАННЯ СТРАХОВОГО РИНКУ УКРАЇНИ**

У статті досліджено основні проблемні тенденції державного регулювання страхової діяльності в Україні, виявлено їх негативний вплив на формування дієвого та повноцінного вітчизняного страхового ринку. Окреслено пріоритетні напрямки реформування державного регулювання страхового ринку України.

Ключові слова: страховий ринок, державне регулювання, страхова діяльність, перестрахування, оподаткування, інтеграція.

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**ПРОБЛЕМНЫЕ ТЕНДЕНЦИИ И НАПРАВЛЕНИЯ РЕФОРМИРОВАНИЯ
ГОСУДАРСТВЕННОГО РЕГУЛИРОВАНИЯ СТРАХОВОГО РЫНКА
УКРАИНЫ**

В статье исследованы основные проблемные тенденции государственного регулирования страховой деятельности в Украине, выявлено их негативное влияние на формирование действенного и полноценного отечественного страхового рынка. Определены

приоритетные направления реформирования государственного регулирования страхового рынка Украины.

Ключевые слова: страховой рынок, государственное регулирование, страховая деятельность, перестрахование, налогообложение, интеграция.

Problem setting. Subject to the sustainable development the competitive market economy is able to function offline, acting as self-regulation and self-organization. However, the market mechanism of the domestic economy is characterized by "market failures" that occur because of the inefficiency of the distribution and usage of economic resources, imperfect competition and institutional environment, financial instability and deepening of economic and political crisis in modern world. Under these conditions, the possibilities of market self-regulation are limited, so they cannot really ensure the effectiveness of the economic development. Therefore there is a need for state intervention into the economic processes reformation and their modernization in conditions of the crisis overcoming. In this context, a particular attention is paid to the development and implementation of effective and balanced mechanisms of state regulation of the insurance market, institutions of which are aimed at the ensuring of economic growth and financial stability of the state, and welfare of its citizens.

"The state should be the guarantor of market economy; the creator of formal restrictions; it should organically fit into the rules of market behavior and do not interfere with market mechanisms" (Jaworska, 2010: 305-309). Because the excessive state intervention into the insurance business may lead to an increase in the insurance cost, the decrease in insurance and reinsurance, lack of insurance premiums and insurance reserves formation. While the imperfect government regulation contributes to the weakening of state control over the activities of market participants that creates conditions for the spread of "schematic" insurance. Thereby the interests of the state should be aimed at balancing the interests of the policyholders and insurers; moreover it is necessary "to look for the economic mechanisms of their coordination and on this basis to define the separation of the state functions and market in the insurance policy of the state" (Bazylevych, 2006: 6-9).

In the insurance theory the problem of state regulation is one of the contemporary ones. This is due, on the one hand, to the insurance market instability, and, on the other hand, to the imperfection of contractual relationships regulation of insurance, contradictions of certain positions of the current insurance legislation and the need to develop the priority directions of phased integration of the national system in the insurance market state regulation and supervision to the international standards.

Latest research and publications analysis. An important contribution to the study of problems of insurance market state regulation was made by such economists as Bazylevych (2006), Hamankova (2009), Dobosh (2010), Zavada (2011), Chernyshov (2011), Jaworska (2010). However, the institutional environment of the insurance market effective functioning is not yet formed, the problems of insurance operations taxation remain urgent; they require development and implementation into the insurance practice of perspective directions of state regulation modernization and insurance supervision.

The research objective is to identify the problematic trends of state regulation of the national insurance market and identify the priority directions of its reformation.

Key research findings. In the crisis, the problems associated with the institutional shortcomings of the insurance market have been escalated, as the introduced anti-crisis measures, which were aimed at guaranteeing the financial security of the state and increasing the role of insurance in the financial stability of the national economy didn't solve the problems of the crisis period. We have systemized the negative trends of state regulation that slow down the development of the insurance market in Ukraine.

The imperfect tax regulation of insurance processes has a negative impact on the formation of a civilized and viable insurance market. Significant changes in financial and economic activities of insurers have taken place with the introduction of the Tax Code of Ukraine of 02.12.2010, which was supplemented and changed several times for the last five years.

In the transitional points of the Tax Code of Ukraine (01. 04. 2011 - 01. 01. 2013) the current tax system was saved, which included a tax rate of 3% of the insurance operations results (Tax Code, 2010). It is advisable to single out a number of controversial points in the regulation of the insurance and reinsurance activities that negatively impact on the insurance market development. In particular it concerns the taxation of insurers' income, according to which the insurance (reinsurance) premiums were the subject to tax both insurers and reinsurers that led to their double (repeated) taxation.

This tax arrangement met the interests of the state due to the usage of insurance and reinsurance as a source of replenishment of the budget, but it contradicted the interests of insurers and reinsurers increasing their tax burden. Under these circumstances the insurers used "schematic" insurance in order to avoid repeated taxation of insurance premiums. It shows that over the time the "schematic" insurance (reinsurance) is reoriented, but its amounts are not changed significantly.

We should note that since 01.01.2013 there have been positive changes, according to which, while determining the tax base from the amount of collected insurance payments, the insurance payments are derived, that are transferred to the reinsurance; it allowed to form a balanced system of insurance business taxation that is able to optimize the interests of the state and insurers. These changes contributed to the avoidance of double taxation, and that's why allowed to lower the reinsurance rates by 3% and it satisfied the insurers' requirements. Accordingly, in 2013, the shares of insurance premiums, which were transferred into the reinsurance, were increased by 2.6 times due to the growth in domestic reinsurance to 246.6%, indicating the interest of the insurers in the placement of the insurance risks to reinsurers residents to protect their property interests and the ability to obtain the additional income in the form of commission (source: Information on the status and development of the insurance market of Ukraine for 2013, 2013).

But the changes to the Tax Code on 1 January 2013 are saved, in accordance with the standards of the Law of Ukraine № 5083-VI "On Amendments to the Tax Code of Ukraine and the State Tax Service in connection with the administrative

reform in Ukraine" dated 05. 07. 2012, including amendments to paragraph 57.1 of Article 57 of the Tax Code regarding the timing of payment of tax liabilities that led to a change in methods of administration of income tax (Tax Code, 2010). The insurer's profit, received during the tax reporting month, is not the base of taxation, but the average value of the insurer's tax payment for 9 months of the previous year. Such innovations on the procedure and methods of taxation of the insurers's profits contradict and violate all principles of the tax policy, economic and social justice, the uniformity of the tax load. It is unknown whether in January or February 2013 the insurer receives incomes in the amount of previous periods.

Thereby, the existing tax regime of insurance and reinsurance operations is virtually changed and a new one is introduced, that leads to an imbalance of fiscal interests of the state, social and economic interests of the insurers (reinsurers). These tax reforms have purely fiscal purpose – to save the tax revenues in the budget at the level of the previous year. Thus, the state creates guarantees of the replenishment of centralized funds, anticipating and deepening the negative trends of economic development in 2013. In our opinion, while determining the approaches to the development of insurance business taxation, it is appropriate, first of all, to take into account its special place in the economic system. Irrational and unfounded tax regulation determines the rising in cost of insurance products, leading to a decrease in sales of insurance and capitalization insurance market. Therefore, the system of taxation of insurance should focus on an optimal combination of fiscal and regulatory functions of taxes with a view to reconciling the interests of the insurance business and the state.

Since January 1, 2015 the insurers face new problems connected with double taxation of their activities. Under the new changes in the Tax Code, the current system of insurance premiums taxation at a rate of 3% is maintained for the insurance companies and at the same time a general system of income taxation from operations (insurance) at a rate of 18% is introduced (Tax Code, 2010). Thus, the insurance premiums are tax base twice: first, when reaching the insurer, and secondly, while the

formation of gross income to calculate the profit before tax. Introducing of such changes absolutely deepens the negative trends in the insurance market.

An important problem of the national insurance market is the low quality of services of the reinsurance operations, that is characterized by imperfect law regulation of the reinsurance contract, no guarantees of timeliness and completeness of payments to reinsurers, poor training and low skill level of market participants.

To improve the contractual relations and quality of the reinsurance services we suggest simplifying the registration procedure of reinsurance contracts, the introduction of which contains no practical value, since it does not provide the specific requirements for the reinsurance contracts, but defines only the obligations of the parties already approved in other legal documents. Such additional legal regulation leads to increasing of regulatory pressure on the insurers due to the complication of the procedure of insurance and reinsurance state regulation.

It is defined that the basic conditions of formation of the management system of insurance and reinsurance services quality are: the creation of an effective mechanism to combat dumping by developing a balanced underwriting policy at the insurance and reinsurance market; providing conditions for the organizations of insurance (reinsurance) pools in Ukraine; quality and transparent information supplying of the market; increasing of the requirements for the assets types and structures, which covered the share capital and reserves of the insurer, and this guarantees the timeliness and completeness of damages due to the insurance contracts.

One of the main directions of the insurance market integration into the world of economic environment is the harmonization of insurance legislation in Ukraine in the context of its conformity with international standards, the determination of the degree of market openness to foreign insurers and the increasing of export-import insurance operations quality. In this context, a significant problem of the national insurance market functioning is the low quality of its information support. The data reflected in the Ukrainian statistical base are insufficiently transparent and traceable. Accordingly, it's practically impossible to reproduce the real processes in the market.

This statistical information is difficult to compare with the market indexes those of other countries without the usage of the additional information and making some adjustments. The auditing activity at the insurance market requires qualitative changes. A large number of small auditing firms in Ukraine often give false conclusions with false and distorted information. For promotion of transparency it is necessary to introduce the general program of transferring the insurance (reinsurance) markets into the international financial reporting standards.

That's because of the common interests of the state, the insurers and their professional associations on improving the legislative regulation of insurance and reinsurance markets, the draft law "On Amendments to the Law of Ukraine "On insurance" № 9614 of 19. 12. 2011 (Draft Law "On Amendments to the Law of Ukraine "On insurance", 2011) has been developed. Certainly, the positive aspect is that the law provides the regulation of relations at the insurance market with the introduction of European standards. The draft law aims to increase the level of insurance and reinsurance protection and is caused by the necessary changes in the regulatory framework associated with Ukraine's accession to the WTO, the adaptation of existing insurance laws to European legislation, the need to improve the monitoring of insurers and to strengthen control over compliance of requirements regarding the insurers' capital and their ability to pay, the feasibility of introducing the European standards of risk classification, the licensing procedures of insurers (reinsurers), international standards of corporate governance and prudential supervision.

Strict selection of risks, increased control of the partners, raising of tariffs and other global trends significantly influenced the structure and quality of insurance business at the Ukrainian insurance market. Accordingly, the tendency to increase their own retention of national insurers is evident, aimed at cost savings for the conclusion of reinsurance contracts. At the same time the institute of reciprocity is especially actualized, which principles prevent the complete competition at the national insurance market and its effective development.

Non-residents, unlike the Ukrainian reinsurers, don't hurry to post their own risks of life insurance at the reinsurance markets of other countries, trying to keep the long-term investments in the national economy. We note that there's no portfolio of domestic reinsurers risk of this type of insurance. On this subject, S. Chernyshov (2011) argues that for the development of the international reinsurance business the companies need to organize a team of professionals able to operate at the foreign markets, to have a high reputation and positive history of cooperation at the foreign markets and the financial stability as at the one of the international rating agencies.

In the current post-crisis period, the national reinsurers must maintain the partnerships with foreign reinsurers and keep their trust, to create a reserve of financial strength in an economic downturn, to develop a clear and balanced and underwriting policy and a marketing line at the reinsurance market. Despite its low capitalization and capacity, some companies have been able to gain the trust and an appropriate level of reputation, and to gain the professional experience at the international reinsurance markets. At the same time the Ukrainian reinsurers face a number of obstacles to their successful development. In particular, it's the lack of state support for the export of reinsurance services, because of the lack of understanding of the reinsurance effectiveness as an important tool for attracting the foreign investments into the country. As a result there's an inadequate state regulation of reinsurance processes, the lack of transparent information support of reinsurers and its inconsistency with international standards of accounting and reporting.

The lack of transparent financial statements according to the international standards (IFRS), that is clear for non-residents from the position of reinsurer's solvency determination and the evaluation of his reinsurance risks and capital, slows the integration of the national reinsurance market into the world insurance space. We note that in Ukraine only a few players at the reinsurance market form the consolidated accounts, applying the international standards and most of them are reporting in accordance with the national legislation. The payments of different indexes differ significantly from their calculations under IFRS, causing unreliable

information support of the national reinsurance market for the international community.

The situation is much more complicated with the introduction of a new legal regime taking into account the risk – solvency standard Solvency II in 2013 in Europe. "An important positive aspect of Solvency II regime is the desire to instill a culture of risk management to the insurers, to encourage them to strategies targeted at higher income on the basis of risk and greater diversification of the portfolio" (Solvency II, 2011). Some positive developments regarding the implementation in practice of the operation of the insurance and reinsurance markets of the international standards for the reporting and new requirements for the solvency of their participants that characterize a new draft law "On Amendments to the Law of Ukraine "On insurance" № 9614 (Draft Law "On Amending Law of Ukraine "On insurance", 2011). Accordingly, the notion of regulatory capital, the calculation of its minimum size was introduced. However, the linear formula is laid in the basis for its calculation which differs significantly from the standard formula of Solvency II; and it creates contradictions between indicators of national and international reporting forms. The usage of this formula in the national practice will increase the number of mergers and acquisitions agreements, as insufficiently capitalized re(insurers) compete to attract the additional capital and attention of big and enough capitalized insurers with diversified portfolios. In our opinion, the introduction of an internal model for the capital formation into the Ukrainian insurance and reinsurance practice is the first step towards the unification of national legislation and international norms of the reinsurance business, but the introduction of Solvency II standards is premature.

Conclusions. Summarizing the mentioned above investigation we outline the priorities of improvement the state regulation of the Ukrainian insurance market in the context of an optimum combination with self-regulation processes at it: to reform the existing method of taxation of the insurers; to set the capital requirements and solvency of the insurers based on the harmonious combination of national practices and monitoring the Solvency I; to simplify the registration procedure of the

reinsurance contracts in the context of avoiding the duplication of existing control functions of the National commission of financial services; to strengthen the control of the national regulator for unfair competition and dumping at the insurance market; to form transparent financial statements in accordance with the international standards, that is clear for the nonresidents from the position of key indicators of insurance and reinsurance business determination; to improve the quality of insurance services in order to guarantee the fulfillment of the obligations under insurance contracts and timely payment of the insurance compensation.

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