The Geneva Papers on Risk and Insurance Vol. 27 No. 4 (October 2002) 638–668

Toward Free Trade in Services: Emerging Insurance Markets in Asia

by W. Jean Kwon*

1. Introduction

The insurance industry plays a crucial role in the economy by allowing individuals and businesses to transfer or finance risks at a substantially lower cost than the value of the subject of insurance. As this efficient use of capital, continuity of insurance protection, depends on the industry's ability to meet its short- and long-term contractual obligations, the government, whether in Asia or elsewhere, closely monitors insurance activity, and tends to adopt rules of regulation that preserve the financial security of the industry as well as that of each insurer.

For this, the government commonly uses a combination of *ex ante* and *ex post* approaches. An *ex ante* approach refers to the practice of setting, often stringent, rules that insurers must abide by. For example, a government may impose rigid market entry barriers, limit the types of ownership structures, detail the scope of insurer operations and investment, and specify premium rates and policy designs. It may operate state-owned insurers, or monopolize reinsurance business. The government may also function as a guaranty mechanism in case of insurer insolvency. In contrast, an *ex post* approach focuses on correcting any distortion once a signal leading to such a distortion has been identified in the market. In the country that relies primarily on *ex post* measures, the regulator sets the minimum entry barriers, but conducts rigorous monitoring of insurer activities. It may allow incumbent insurers to operate and invest freely, but subject them to stringent solvency margins or risk-based capital standards. Self-regulatory approaches such as corporate governance and self-regulation by industry associations are increasingly observed in the markets subject to *ex post* regulatory measures (Kwon, 2001).

Simply adopting an *ex post* approach for insurance regulation does not guarantee that the market will mature and become competitive. A mature market calls for regulation and supervision of international standards. The market need be served by financially sound and technically robust insurance entities. Well developed infrastructure should exist in the economy for optimal supply of and demand for insurance. When all these elements are found in the market, policyholders' interests can be best protected and a further growth of the insurance industry is expected. Whether recent changes in insurance regulation and

---

* Associate Professor of Insurance, the School of Risk Management, Insurance and Actuarial Science, St John's University. The discussion in this paper is based on author's compilation of latest information from a number of reliable sources as well as comments from regulatory authorities and local experts in selected countries. Nevertheless, part of the information in this paper might not correctly reflect the regulatory environments of certain countries at the time of publication. The author gratefully acknowledges valuable comments from numerous academicians, industry professionals and regulators including Ramesh Raj Bhattarai, Vida Chiong, Ray Chen, Shu-Chuan Chen, Mark Dorfman, Tim Fisher, Robert Gibbons, David Hatton, Haji Abdul Hamid Haji Janudin, Yu Jin, M. Kanapathipillai, Le Hoai Nam, Un Taing Im, and Harold D. Skipper.

© 2002 The International Association for the Study of Insurance Economics.
Published by Blackwell Publishers, 108 Cowley Road, Oxford OX4 1JF, UK.

supervision in emerging Asian countries are in line with these requisites warrants examination.

This paper comprises three parts, inclusive of this introductory part. The next part describes current regulatory and supervisory environments in 19 Asian markets.[1] They are grouped into three cohorts: (1) Greater China consisting of the People's Republic of China, Hong Kong, Macau and Taiwan; (2) ASEAN member countries comprising Brunei Darussalam, Cambodia, Indonesia, Laos, Myanmar, Malaysia, the Philippines, Singapore, Thailand and Vietnam; and (3) Indian Ocean countries such as Bangladesh, India, Nepal, Pakistan and Sri Lanka. In the last part, the author summarizes his findings, and provides his conclusions and recommendations.

2. Country studies[2]

The discussion in this part is divided, whenever possible, into four segments for each country. The first segment deals with market access regulation. Openness of the market to local private firms and foreign insurers, licensure requirements including initial capital requirement, and other conditions warranting some elaboration are discussed in this segment. The next segment discusses the solvency regulation that licensed insurers in the country must abide by. The third segment describes investment guidelines, including accounting principles, applied to insurers operating in the country. The last segment summarizes market conduct regulation with respect to insurers' pricing, product designs, reinsurance arrangement, and policyholder protection.

Greater China

The People's Republic of China (PRC) and Taiwan are export-oriented countries, but in the past they allowed foreign firms somewhat limited access to their local markets. The resulting sizeable trade surpluses became a searing issue, especially on their application to become WTO members. Both countries have since made considerable changes, including amendment of insurance laws, in their regulatory approaches. As a result, the insurance markets in the PRC and Taiwan have become, to a certain degree, privatized, liberalized, and deregulated. Hong Kong and Macau, which remain independent of the PRC in managing their economies for 50 years from the date they became part of the PRC, continue to maintain relatively liberal insurance markets. The administrators in these special administrative regions continue to introduce new guidelines that can enhance the competitiveness of the local insurance markets.

People's Republic of China (the PRC)

The PRC introduced the Insurance Law of the People's Republic of China on 30 June 1995. This law covers key regulatory issues, but is short of providing unequivocal, or transparent, guidelines to specific operative matters of insurance business. The government

---

[1] Japan and Korea, which are OECD member countries, are not examined in this study. Not investigated either in this study are the Maldives, Mongolia and North Korea for lack or unavailability of reliable information.

[2] Discussion in this part is based on the author's monographs published in 2001 and 2002 by the International Insurance Foundation [*www.iifdc.org*].

© 2002 The International Association for the Study of Insurance Economics.

clarified some of this gray area in the WTO protocol of Accession of China and through issuing additional regulations, e.g., the Regulations on Administration of Foreign-invested Insurance Companies of 2001. The China Insurance Regulatory Commission (CIRC), which was created in November 1998, regulates the insurance industry.

Market access regulation

A new domestic insurer can be a solely state-owned firm or a stock company. As a WTO member country, the PRC no longer applies the economic needs test. An applicant of insurance business is required to raise a minimum initial (registered) capital of 500 million yuan to carry on insurance business on a nationwide basis, or 200 million yuan (renminbi) to operate within a designated territory. No direct insurers are allowed to hold licensure for both life and non-life insurance businesses.

The insurance law and its related regulations prescribe that the foreign applicant must have been in insurance business for more than 30 years at the time of application, and its total assets at yearend prior to submission of the application must be greater than U.S.$5 billion. The applicant must have had a representative office in the PRC for two consecutive years.

Qualified foreign insurers are permitted to establish a branch, or create a joint venture with up to 51 per cent ownership. This restriction will be removed within two years after the PRC's accession to the WTO, and foreign insurers will then be permitted to operate through their wholly owned subsidiaries. As per life insurance business, foreign insurers can operate only as a joint venture with up to 50 per cent equity ownership of the joint venture. Foreign life insurers may be allowed to operate through wholly owned subsidiaries within five years after the PRC's accession to the WTO.

Solvency regulation

A licensed insurer must maintain a minimum solvency margin commensurate with the size of its business. For property insurance and short-term personal insurance business, the margin must be the greater of: (1) 18 per cent of retained premiums less than 100 million yuan, plus 16 per cent of retained premiums greater than 100 million yuan, both for a given accounting year; or (2) 26 per cent of the average annual claims payments made in the previous three years that is less than 70 million yuan, plus 23 per cent of the same claims basis that is more than 70 million yuan.

The minimum solvency margin for long-term personal insurance business is the sum of the following two formulae: (1) 4 per cent of liability reserves for ordinary life insurance business plus 1 per cent of liability reserves for investment-linked business; and (2) 0.1 per cent of the amount of insurance for fixed-term life insurance risk with the coverage period less than three years, 0.15 per cent of the amount of insurance for fixed-term life insurance risk with the coverage period of three to five years, and 0.3 per cent of the amount of insurance for fixed-term life insurance risk with the coverage period greater than five years as well as for other types of risks.

Financial and accounting regulation

All insurers must maintain an outstanding loss reserve for the amount of insurance indemnity, or the amount of the insurance benefits for reported-but-not-yet-settled claims and IBNR claims, subject to a 4 per cent limit based on the actual claims payments made during the relevant year. Additionally, all non-life insurers must set aside 50 per cent of the premiums

© 2002 The International Association for the Study of Insurance Economics.

retained for the current year as a reserve for future claims. The life insurer must set aside to its policy reserve an amount equaling the total net value, determined actuarially, of the total life insurance policies in force. When preparing financial statements, insurers may use generally accepted accounting principles.

The insurance law is strict and confines the areas of insurer investment to bank deposits, government bonds, financial bonds, and central enterprise bonds designated by the CIRC or by the State Council. The insurance law gives the regulator an authority to set the exact percentage of an insurer's total fund allocated to each permitted area. However, the CIRC has loosened this regulation over the years.

Market conduct regulation

The current Insurance Law states that an insurer must secure approval from the regulator when it expects changes of shareholders holding more than 10 per cent of the company's share. The CIRC can set the (premium rate and policy) standards for the main types of risks in commercial insurance, and the standards can be revised according to prevailing market conditions. For property insurance business, the premium retained for the current year cannot exceed more than four times the sum of the insurer's paid-up capital plus its accumulated reserve fund. Property insurers may accept large risks over their permitted capacity as long as they cede the excess amount of risk over their capacity to a reinsurer or reinsurers.

Compulsory cession to the national reinsurer remains in force for four years after the PRC's accession to the WTO. Currently, non-life insurers are subject to compulsory reinsurance cession of 20 per cent of their direct insurance business in non-life lines as well as personal accidental insurance and health insurance to the Chinese Reinsurance Company. The percentage will be reduced to 15 per cent from 2003, to 10 per cent from 2004, and to 5 per cent from 2005. From year 2006, no compulsory cession will be imposed.

Hong Kong, Special Administrative Region

The Hong Kong Government established in 1990 the Office of the Commissioner of Insurance (OCI) as the regulatory body of the insurance industry. The regulatory framework for the industry is prescribed in the Insurance Companies Ordinance (Chapter 41) of 1983. This ordinance has been amended several times, the latest in 2000.

Market access regulation

Only authorized companies, Lloyd's, and associations of underwriters approved by the OCI can carry on insurance business in or from Hong Kong. Many of the regulatory conditions for admission deal with a proper and fit person rule and readiness of the applicant for sound financial and operational management of the proposed business. The presence or availability of reinsurance arrangements is also a condition to complete the application. An applicant for general business or long-term business is required to have a minimum paid-up capital of HK$10 million. For composite insurance business or any statutory insurance business, the minimum paid-up capital is HK$20 million. The minimum paid-up capital for captive insurance business is HK$2 million.

© 2002 The International Association for the Study of Insurance Economics.

Solvency regulation

Insurers must maintain an excess of assets over liabilities of not less than the required solvency margin. The solvency margin of the non-life insurer is expressed in terms of the relevant premium income (e.g., the greater of the annualized premium income, net of reinsurance, or 50 per cent of the annualized premium income) or the relevant claims outstanding (e.g., the greater of the claims outstanding, net of reinsurance recoverable, or 50 per cent of the gross claims outstanding plus any additional provision of unexpired risks). For long-term insurers, the margin is determined by the greater of (1) HK$2 million, or (2) an amount specified under the Insurance Companies (Margin of Solvency) Regulation of 1995 (which is generally 4 per cent of the mathematical reserves plus 0.3 per cent of the capital at risk). The minimum margin of solvency for the composite insurer is the sum of the minimum requirements for each class of business described above.

Financial and accounting regulation

The Insurance Companies (General Business) (Valuation) Regulation provides bases for the valuation of the assets and liabilities of insurers carrying on general business, other than captive insurers. Besides, the law requires each non-life insurer, excluding professional reinsurers and captive insurers, to maintain its assets in Hong Kong of an amount that is not less than the aggregate of 80 per cent of its Hong Kong liabilities, net of reinsurance, plus the relevant amount pertaining to its Hong Kong business. If the insurer's reinsurance premium exceeds 50 per cent of the gross premium, it must maintain assets in Hong Kong that reflect 40 per cent of its Hong Kong liabilities and the relevant amount pertaining to its Hong Kong business. Exceptions to these rules may be made.

The Insurance Companies (Determination of Long Term Liabilities) Regulation sets out the bases for the determination of the amount of long-term business liabilities. Hong Kong does not have any specific guidelines related to investment activities of insurers.

Market conduct regulation

Any person entitled to exercise, or wishing to control the exercise of 15 per cent or more of the voting rights of an authorized insurer should secure the regulatory authority's consent. All licensed insurers are required to notify the Insurance Authority of an appointment of a new director. Insurers are required to maintain adequate reinsurance arrangements. However, there are no specific guidelines or regulations related to this provision.

Macau, Special Administrative Region

The government created in 1989 the Monetary and Foreign Exchange Authority of Macau, now known as Monetary Authority of Macau (AMCM), as the new regulator of the financial services sector. From April 2000, AMCM assumed the responsibility of managing the reserve fund of the Macau Government, and has since supervised monetary and financial operations in Macau.

Market access regulation

A licensed insurer can be a locally incorporated company or a branch of a foreign insurer. The minimum required capital is 30 million patacas for life insurance business or 15 million patacas for non-life insurance business. If the application is for reinsurance operation, the

© 2002 The International Association for the Study of Insurance Economics.

minimum capital rises to 150 million patacas for life business, or 100 million patacas for non-life business. In the case of an application for branch operation, the ordinance requires a minimum establishment fund of 7.5 million patacas for life insurance business, or 5 million patacas for non-life insurance business. AMCM additionally requires that the share capital of the head office of the branch applicant should not be less than the minimum capital required for a locally incorporated insurer.

Solvency regulation

Authorized insurers must maintain a margin of solvency that is sufficiently large to meet their insurance obligations arising from underwriting risks in Macau. The required margins are determined based mainly on the annual gross premium during the preceding year, net of returns and cancellations, of the insurer. However, if an insurer or reinsurer experienced abnormal losses during the preceding three consecutive years or during any three years of the preceding five years, its minimum margin of solvency is twice the usual amount. The required margin of solvency for a life insurer is based on the mathematical reserves and the amount of capital at risk – the amount payable on death less mathematical reserves for the coverage. The margin also varies according to the line of business the insurer writes.

Financial and accounting regulation

Insurers must maintain, at minimum, two technical reserves: claims reserve and mathematical reserve (for life business) or unearned premium reserve (for non-life business). The claims reserve reflects the insurer's foreseeable future claims liability, including claims incurred but not reported. The mathematical reserve corresponds to the difference between the actual values of reciprocal liabilities of the insurer and its insureds. For the calculation of unearned premium reserves, non-life insurers may use a pro-rata method for each outstanding individual policy. Life and non-life insurers must guarantee the amounts for their technical reserves using their assets located in Macau.

Market conduct regulation

Authorized insurers in Macau are free to assume reinsured risks from or cede their risks (as long as such risks are within the class of business for which they are licensed) to insurance or reinsurance companies licensed in the territory or elsewhere. No person, whether an individual or a corporate body, is permitted to hold a qualified shareholding – 10 per cent, or more, of the share capital or voting rights – or any increase of shareholding by 5 per cent of the capital, or of the voting rights, without prior approval of AMCM.

Taiwan, the Republic of China (Taiwan)

Taiwan continues its privatization, liberalization and deregulation processes. It introduced the Financial Institutions Merger Law in 2000, the Financial Holding Company Law in 2001, and the Financial Supervisory Board Law in 2001. Under the Financial Supervisory Board Law, a single supervisory authority oversees operations in the banking, insurance, securities, and futures markets. The Financial Holding Company Law offers a legal basis for the creation of financial holding companies that can offer banking, insurance, securities and finance services through their subsidiaries. This law also permits joint-marketing efforts among the subsidiaries of a financial holding company.

© 2002 The International Association for the Study of Insurance Economics.

Market access regulation

An authorized insurer can be structured as a stock company or as a cooperative (mutual) company. A new insurer must have a paid-up capital of NT$2 billion. Foreign applicants must have earned an A-rating from an approved international rating agency.[3] The minimum paid-up capital is NT$50 million for foreign branch operation; if the application is by a foreign mutual insurance company, the parent company must have net worth of at least NT$2 billion. A direct insurer may engage in reinsurance business, but cannot hold licensure concurrently in life and non-life classes.

Solvency regulation

The insurance law is silent about the minimum solvency margin requirement *per se*, but has at least three relevant provisions. The maximum amount of insurance, net of reinsurance, of an exposure cannot exceed 10 per cent of the insurer's policyholder's surplus. The insurer must maintain its excess of admitted assets over liabilities at three times the amount of the guarantee fund it has posted with the national treasury. Finally, the regulator may use a risk-based capital system as a tool to measure capital adequacy of insurers.

Financial and accounting regulation

The minimum reserve for fire insurance business is 40 per cent of the insurer's retained premium during the year of business. It is 20 per cent of the "entire" premium income for marine cargo insurance. For marine hull insurance, the minimum is 60 per cent of the entire premium income retained. Insurers operating in automobile damage insurance, liability insurance, guarantee insurance, and other types of property insurance must maintain a minimum statutory reserve of 50 per cent of their entire premium income retained. These minimum reserve requirements apply only to insurance policies having a term of one year or less. For policies having a longer policy period, the regulatory authority may impose different reserve requirements. Non-life insurers must maintain loss reserves. The rules regarding policy reserves, which apply to personal insurers, are a little more complex. Personal insurers are additionally subject to statutory reserve requirement rules based on their claims experience. The insurance law is silent regarding accounting principles that insurers may use.

Insurers are permitted to invest their funds – owner's equity and various policy reserves – in marketable securities, real estate, lending, foreign investment, as well as special projects and public investment (subject to the approval of the regulatory authority). No insurer is permitted to borrow money for any other purposes than paying for major claims. Neither is any insurer permitted, unless approved by the regulatory authority, to use its assets as collateral for the loan. An outstanding loan that an insurer owes must be repaid within five months.

Market conduct regulation

Insurers can now file for approval for premium rate formulae, policy clauses, insurance application forms, and other relevant materials prescribed by the regulator. There are

[3] The Regulations on Granting Special Approval and Administration on Foreign Insurance Companies (amended in May 2001).

© 2002 The International Association for the Study of Insurance Economics.

exceptions. Insurers in Taiwan participate in several funds including the third-party automobile liability insurance fund and the residential earthquake insurance fund.

Association of Southeast Asian Nations (ASEAN)

In the ASEAN circle, there are economically advanced countries as well as countries where the population struggles to overcome poverty. With an exception of Brunei, Malaysia, Singapore and Thailand, other ASEAN countries generate less than U.S.$5,000 GDP *per capita* (purchasing power parity adjusted). This implies that the insurance industry has yet to develop and the current level of consumption of insurance remains low in most ASEAN countries. Nevertheless, signs of governments' moves toward free trade in insurance service are increasingly observed in the region.

Negara Brunei Darussalam (Brunei)

Brunei allows only *takaful* insurers, insurers offering products complying with Islamic principle, to operate as composite insurers.[4] The only insurance-related law in this country is the Motor Vehicles (Third-Party Risks) Act of 1998. The Financial Institutions Division (FID) of the Ministry of Finance monitors and supervises insurance activities in Brunei. Its major activities include granting licenses to insurance business applicants, although no new insurer has been registered since 1984. A non-life insurance business applicant must meet the minimum paid-up capital of B$1 million. Once admitted, it must maintain a solvency margin of 20 per cent based on premium income, net of reinsurance, of the previous year. For insurers writing motor insurance business, the ministry requires a deposit of B$1 million with the government.

The FID does not strictly direct how non-life insurers price their products or maintain their insurance funds for most lines of insurance. Instead, the regulator, through its guidelines on the accounting procedures, requires non-life insurers to calculate unearned premium reserves pro-rated to the period of insurance coverage, to estimate IBNR losses based on past experience, and not to discount their outstanding claims (Chua, 1999). Non-life insurers must use the lower of the book value or market value when valuing their investments.

Kingdom of Cambodia

The Insurance Law, adopted in June 2000, prescribes that an entity must seek approval from the Ministry of Finance before it commences insurance business. In the past, certain projects and assets could be insured overseas. The insurance law no longer allows such practises, and all projects and assets located in Cambodia must be insured locally and by a licensed insurer. This provision is added to the law as a measure to stop outflow of premiums from the country.

The insurance company in Cambodia is subject to some provisions of the country's tax law, which was amended in 1997. The law prescribes that the insurer residing in Cambodia be subject to 5 per cent income taxes based on its gross premiums for risks in Cambodia. For income from non-insurance activities, insurers are subject to income taxes of generally 20 per

[4] See Kwon and Maysami (1999) for an analysis of *takaful* insurance principles and operations.

© 2002 The International Association for the Study of Insurance Economics.

cent of their profits. The insurance industry is in its infancy with only one state-owned insurance company, Caminco.

Republic of Indonesia

Market access regulation

The Directorate General for Financial Institutions with the Ministry of Finance regulates the insurance industry. The minimum paid-up capital is 2 billion Indonesian rupiah for domestic life insurers, or 4.5 billion rupiah for joint ventures in life business. In non-life insurance, it is 3 billion rupiah for domestic insurers, or 15 billion rupiah for joint ventures. Locally incorporated reinsurers are required to have a minimum paid-up capital of 10 billion rupiah; for other reinsurers, the amount increases to 30 billion rupiah.

A foreign insurer wishing to enter this local market must first locate an Indonesian partner, and have an equity capital of at least twice the amount of its investment in the joint venture. The local partner must have been operating for at least two years while satisfying the authority's requirement for solvency test. The applicant must submit a plan describing how the foreign partner's ownership in the joint venture will be reduced over a specified period of time. In particular, a registered joint venture must limit its foreign ownership initially to 80 per cent of the total share, and gradually, i.e., within 20 years, reduce it to no more than 49 per cent of the total share.

Solvency regulation

Life insurers must maintain a solvency margin of at least one per cent of premium reserves for life insurance and 10 per cent of net premium for health and accident insurance. Non-life insurers should meet a solvency margin being at least the sum of the initial minimum capital and 10 per cent of net premiums. Non-life insurers are not permitted to assume any risk if the coverage amount exceeds 10 per cent of their equity. The total amount of premiums, net of reinsurance, that non-life insurers can write is limited to 300 per cent of their equity. The Ministry of Finance may also employ risk-based capital models to determine solvency requirements of insurance companies operating in Indonesia.

Financial and accounting regulation

In the case of a life insurer, its total investments, excluding investment in mortgage loans, must be at least equal to its technical reserves. It must maintain a premium reserve, the amount of which is determined in accordance with the ministry guideline, as well as a liability provision for future policy benefits as approved by a registered actuary. In the case of non-life insurers, the total investments, excluding investment in mortgage loans, should be at least equal to the sum of the technical reserves plus 25 per cent of equity. As with valuation of invested assets, insurers must use book value or market value, the choice being dependent on the type of invested asset.

Market conduct regulation

An insurer must obtain prior approval from the regulator to open a branch office. It is not permitted to own equity of an insurance brokerage firm or agency. Besides, the Indonesian Insurance Council, an industry association, publishes a tariffs book for various non-life lines

© 2002 The International Association for the Study of Insurance Economics.

of insurance that insurers must abide by. Non-life insurers are subject to commission limits of 15 per cent for brokers and 10 per cent for agents.

Direct insurers, especially non-life insurers, must have a treaty reinsurance arrangement with at least one reinsurer, and retain at least 30 per cent of the original risks based on premiums. They may place risks to offshore reinsurers, provided that those reinsurers, among others, have a (reciprocal) treaty agreement with at least one domestic reinsurer in Indonesia, and have a paid-up capital at least equaling the minimum capital required for domestic joint venture reinsurance companies, i.e., 30 billion rupiah.

Laos People's Democratic Republic

It was not until in 1990 that the government implemented the first, albeit uncomplicated, Insurance Law. Nor did Laos have an insurer until the government established in 1992 a joint venture insurance company, *Assurances Générales du Laos* (AGL). AGL was given a three-year monopoly, and since 1995 has been a *de facto* monopoly as no other insurer has been licensed in the country (Ministry of Finance, 1999). The State Property Directorate functions as the regulatory authority of the insurance industry.

The Insurance Law does not limit the types of insurance products that an insurer can sell, but requires it to obtain prior approval for premium rates and policy conditions from the ministry. No specific accounting principle for the insurance industry exists, and AGL uses a generally accepted accounting principle for its financial statements.

Malaysia

The Ministry of Finance is the *de facto* regulatory supervisor of the insurance industry, but has long delegated the duty of administering the insurance law to Bank Negara Malaysia (BNM), the central bank of Malaysia. A challenge that most Malaysian insurers face is perhaps the government's market consolidation plan through mergers and acquisitions. BNM said in March 2000 that there would be 10 to 15 insurers left after completion of the consolidation of the industry by 2003.

Market access regulation

BNM requires, from September 2001, a minimum paid-up capital of RM100 million for insurance business in the country.[5] There are two specific provisions regarding foreign investment in the Malaysian insurance market. The first is that BNM allows foreign investors to hold up to 30 per cent of ownership equity of any Malaysian insurance company. Under the second, the Insurance Act made it mandatory for all branches of foreign insurers to be domesticated, i.e., locally incorporated as a subsidiary, by June 1998.

Solvency regulation

A licensed direct insurer and a reinsurer should maintain at all times a fund margin of solvency of RM50 million and RM10 million, respectively, for each class of business. In addition, it must maintain an insurance fund for each class of its insurance business. The

[5] For branches of foreign insurers, the minimum capital is calculated as the surplus of assets over liabilities.

© 2002 The International Association for the Study of Insurance Economics.

Insurance Act additionally prescribes that all licensed insurers maintain admitted assets of no less than the sum of the liabilities of the insurance fund and the fund margin of solvency.

Financial and accounting regulation

Insurers operating in Malaysia are subject to the *Bumiputra* investment recommendation that the Malaysian Government made in its 1996–2000 National Development Plan. In line with this recommendation, insurers must maintain, unless relief is granted, at least 30 per cent of their investment in *Bumiputra* share, that is, ownership share by ethnic Malay.[6] Additionally, licensed insurance players must obtain prior approval from BNM for any changes in their ownership shares. If such a change concerns an acquisition or sale of an interest in excess of 5 per cent of the shares of a licensed insurer, the insurer must obtain prior approval directly from the Ministry of Finance.

Market conduct regulation

The insurance regulator maintains the Insurance Guarantee Scheme Fund, in which all non-life insurers participate. The Insurance Act and the Insurance Regulations include provisions regarding insurer expenses and premium rates. BNM also issued two guidelines on insurers' operating costs. In particular, the General Insurance Association of Malaysia sets premium rates for fire and motor insurance businesses, and its member non-life insurers must abide by the tariff rates. All insurers must comply with the act when designing their insurance application forms, contracts and marketing brochures. BNM also sets the maximum percentage of agency commissions on insurance policies.

Union of Burma (Myanmar)

The Insurance Business Supervisory Board, formed in 1996, is the regulatory authority of the country. This body is with Myanmar Insurance, and its members are drawn mainly from Myanmar Insurance, Central Bank of Myanmar and other government authorities. The Insurance Business Law of 1996 and the Insurance Business Rules of 1997 prescribe that an applicant of insurance business must file an application to the board. Separately, it must obtain approval of its investment plan from the Myanmar Investment Commission before it can commence insurance operation. The regulator requires all insurers to maintain a capital of at least 20 million kyats for life insurance, or 200 million kyats for non-life insurance. Myanmar currently does not have either solvency requirement guidelines or investment guidelines.

All insurers are required to use only the insurance application and policy forms approved by the regulatory authority. Life insurers must also obtain prior approval from the board for any changes in life insurance surrender values, premium rates and commission structures. Finally, insurers operating in Myanmar must establish a policyholders' protection fund to protect mainly owners of life insurance policies.

Republic of the Philippines

The Philippines maintains the principle of free enterprise and emphasizes the role of the private sector for its economic development. The Insurance Commission (*Komisyon ng*

[6] This recommendation does not apply to Malaysian reinsurance branches of foreign companies.

© 2002 The International Association for the Study of Insurance Economics.

Seguro) regulates and supervises the insurance industry in accordance with the Insurance Code.

Market access regulation

In the Philippines, a firm may engage in insurance business by owning voting stock of an existing domestic insurer, investing in a new insurance or reinsurance company in the country, or establishing a branch. Up to 100 per cent foreign ownership of local insurance and reinsurance companies is permitted in the country. Currently, the minimum paid-up capital for direct business is 75 million pesos for direct business or 150 million pesos for reinsurance business.

As with foreign insurance operation, the licensing guideline issued by the Department of Finance in 1994 states that the minimum capital varies depending not only on the type of business, direct or reinsurance, but also on the percentage of foreign ownership. Besides, the Insurance Commission examines a number of factors when reviewing applications by foreign insurers (e.g., reciprocity rights that Philippine insurance entities can enjoy in the applicant's country). The foreign applicant must have at least ten years' experience as of the date of application. To qualify as a branch or as a new company incorporated in the Philippines, the applicant must be widely owned or publicly listed in its country of origin, unless it is majority-owned by the government. A new foreign insurer is not allowed to hold a composite license. It may, however, apply for a separate license for each of life and non-life business.

Solvency regulation

All insurers must maintain the margin of solvency prescribed in the Insurance Code. For the life insurer, the total admitted assets must be greater than the sum of the total liabilities plus paid-up capital plus revaluation reserves, and the difference must be the greater of (1) 0.5 million pesos, or (2) 0.2 per cent of the total amount of all policies (except term life insurance) for the preceding year. In the case of a non-life insurer, the amount should be the greater of (1) 0.5 million pesos, or (2) 10 per cent of the total amount of net premiums written during the preceding year. In the case of a foreign branch insurer or reinsurer, its head office must guarantee prompt payments of all liabilities of the Philippine branch.

Market conduct regulation

An insurer must obtain approval from the Insurance Commission before it commences marketing an insurance product. Life insurers are required to obtain approval from the commission of the premium rates for their life insurance products. In contrast, the Philippines Insurance Rating Association recommends premium rates for non-life insurance tariff lines, notably, motor insurance and bond (surety) insurance. All non-life insurers are a member of this association and must abide by the recommended premium rates.

Republic of Singapore

The Insurance Department of the Monetary Authority of Singapore (MAS), the *de facto* central bank of Singapore, is responsible for the regulation and supervision of the insurance industry. Singapore last amended its insurance law in October 2000.

© 2002 The International Association for the Study of Insurance Economics.

Market access regulation

In March 2000 Singapore reopened its door to direct insurers, and lifted the then 49 per cent restriction on foreign ownership of locally incorporated insurers. New applicants can still be subject to a needs test, e.g., commitment to Singapore's development as a regional insurance hub and international financial center, a practice short of full liberalization of the insurance market.[7] A qualified applicant in direct insurance and reinsurance business must raise a minimum paid-up capital of S$25 million. The minimum paid-up capital applied to captive insurers is S$400,000. The department may grant specialized licenses, holders of which can operate in selected lines of insurance (e.g., financial guaranty insurance).

Solvency regulation

The solvency margin requirement comprises two elements, the fund margin of solvency and the company margin of solvency. To meet the margin requirement, an insurer must set up and maintain a separate insurance fund for each class of insurance business, which is further segmented into the Singapore Insurance Fund for domestic businesses and the Offshore Insurance Fund for offshore businesses. Specific solvency margin requirements exist for each of these insurance funds. To meet the other solvency margin, the company margin of solvency, all insurers other than captive insurers must maintain S$5 million per class of business, or S$10 million for both classes. Captive insurers are subject to a company fund margin of S$400,000.

Financial and accounting regulation

Non-life reinsurers must maintain an amount not less than 25 per cent of the premiums of marine and aviation policies, and 40 per cent of the premiums in other policies. They are not allowed to discount their loss reserves. Direct life insurers are subject to the statutory minimum valuation basis for computing their actuarial reserves. The Insurance Regulations of 1999 prescribe investment limits of the SIF by asset type and exposure. For example, an insurer may invest up to 45 per cent of the fund in equities, 30 per cent in overseas assets, and 25 per cent in real properties. There is no specific investment requirement for offshore business, but insurers are expected to exercise prudence in their investments. Some exceptions exist.

Market conduct regulation

Direct insurers must have suitable reinsurance arrangements at all times, and their reinsurance partners must have good securities. Insurers operating in Singapore must obtain approval of their principal officers and directors from the Insurance Department. In cases of life insurers, they must also seek approval for the appointment of appointed actuary.

Kingdom of Thailand

The Department of Insurance of the Ministry of Commerce is the regulator and supervisor of the insurance industry. The department encourages insurance companies to be

[7] The other criteria for entry of new direct insurers would be their (1) domestic and international rankings, (2) present and past credit ratings, and (3) track record and reputation with regard to compliance with regulations and the strength of internal control systems.

© 2002 The International Association for the Study of Insurance Economics.

responsible for their intra-company activities via corporate governance and for their inter-company activities via self-regulatory bodies.

Market access regulation

The Thai Government is liberalizing its insurance market in three phases. During the first phase, it amended Life and Non-life Insurance Acts, and permitted new domestic insurers to form a joint venture with up to 25 per cent foreign ownership. The Department plans to allow foreign equity participation up to 49 per cent once the existing insurance laws have been amended. After another five years from the date the new laws have become effective, the foreign ownership restriction is likely to be eliminated. Newly licensed life and non-life insurers are now required to raise a minimum paid-up capital of 500 million baht and 300 million baht, respectively.

Solvency regulation

Life insurers are required to maintain a capital fund of not less than 4 per cent of the insurance reserve, or not less than 500 million baht, whichever is greater. However, the government has placed an interim measure such that an insurer may meet a capital fund of not less than 300 million baht within three years and increase the fund to 500 million baht within five years from the date of implementation of this new capital requirement.

Non-life insurance companies must maintain a capital fund of not less than 20 per cent of net premiums written in the previous year. Non-life insurers are also given relief such that they meet only 200 million baht within three years and increase the fund to 300 million baht within five years from the date of implementation of this new capital requirement. The Insurance Department may impose additional requirements on Thai branches of foreign insurers.

Financial and accounting regulation

The Ministry of Commerce introduced in 1993 a guideline that basically requires insurers to make investment within Thailand. Insurers may invest outside Thailand in shares and debentures of reinsurance companies incorporated under ASEAN or ESCAP agreements or in others for which they have obtained approval from the authority.

Market conduct regulation

Several regulatory and supervisory measures regarding insurer operation are in place in Thailand. First, in 1999 the government banned insurers from operating life and non-life insurance businesses concurrently. Second, non-life insurers are subject to tariff rates for their motor insurance business. Fire insurance premiums are also subject to tariff rates. Third, all direct insurers have entered into a gentlemen’s agreement to cede on a quota share basis at least 5 per cent of their assumed risks in fire, marine, transportation, and miscellaneous insurance to the Thai Reinsurance Public Company. They must also maintain a proper reinsurance arrangement if the aggregate fire risk they have assumed in a geographical zone exceeds 10 per cent of the solvency margin, or the total risk in their motor business portfolio exceeds 10 per cent of the solvency margin, or the risk of any individual policy exceeds 10 per cent of its surplus.[8]

---

[8] The regulatory authority may have revised its rules regarding reinsurance transactions by the time of publication.

© 2002 The International Association for the Study of Insurance Economics.

Socialist Republic of Vietnam

Market access regulation

According to the first Insurance Law of the country, which was introduced in December 2000, an entity wishing to do insurance business may file an application with the Ministry of Finance. A new insurance company may be formed as a mutual company, a stock insurer, a joint venture insurer, or a wholly-owned subsidiary. Composite insurance business is not permitted in Vietnam. The minimum paid-up capital required is 70 billion Vietnamese dong for Vietnamese non-life entities, or U.S.$5 million for foreign non-life firms. For life insurance business, the minimum required capital is 140 billion dong for Vietnamese insurers, or U.S.$10 million for foreign-owned insurers. All insurers must make a security deposit, 5 per cent of the required capital, with a licensed bank in Vietnam.

Solvency regulation

All insurers must maintain assets in excess of liabilities by an amount of no less than the sum of the paid-up capital plus compulsory reserve funds and retained profits. In addition, they must meet the following requirement: for non-life insurers, 20 per cent of the total premiums for the risks they retained from the previous financial year; or for life insurers, 0.1 per cent of the aggregate coverage of all policies in force during the previous financial year.

Market conduct regulation

There are several guidelines regarding insurer operations and market conduct. For example, insurers are not permitted to open more than one branch in a city. Non-life insurers are subject to compulsory session, presumably 20 per cent of their assumed risks on a quota share basis, to the Vietnamese National Reinsurance Company. The Ministry of Finance plans to phase out this cession requirement over the next few years.

In the case of foreign insurers, they are committed to investing all premium revenue in Vietnam, and must contend with public doubts over the stability of Vietnam's official currency. Wholly foreign-owned insurers may remit overseas their retained profits after meeting all reserve requirements. Foreign parties of joint venture insurance companies may also remit overseas the amount of distributed profits after meeting all reserve requirements.

Indian Ocean countries

Bangladesh, India, Nepal, Pakistan and Sri Lanka share some commonalities. The governments of these countries nationalized key industries in the early 1970s, but since the 1990s have begun, or plan to begin, to privatize state-owned enterprises. They have also relaxed foreign currency controls, reduced many other foreign trade barriers, and opened, albeit partially, their financial services markets. The insurance market in each of the countries is thus in transition from a nationalized market to a partially private sector-driven market. These changes toward free trade in insurance services – privatization, liberalization and deregulation of the industry – can further the development of the Asian insurance market.

People's Republic of Bangladesh

The Department of Insurance of the Ministry of Commerce is the regulatory authority of the insurance industry. The regulatory and supervisory guidelines are more or less governed

© 2002 The International Association for the Study of Insurance Economics.

by the Insurance Corporation (Amendment) Act and the Insurance (Amendment) Act both of 1990.

Market access regulation

The Department of Insurance requires a minimum paid-up capital of 75 million taka for life insurance business, or 150 million taka for non-life insurance business. It may grant licensure to a new insurer if it has raised at least 40 per cent of the required capital. The insurer with this special grant must generate the remaining 60 per cent from public share subscriptions within three years of operation, and its sponsors must guarantee the future public share subscriptions. The market is still closed to foreign insurers, except American Life Insurance Company that offers insurance coverage in selected life insurance lines.

Other regulation

No provisions specific to solvency regulation are found in Bangladesh. Instead, the regulator continues to impose stringent investment guidelines. The regulatory authority also subjects insurers to statutory accounting guidelines. As such, life insurers are required to estimate and reserve their policyholders' liabilities based on an actuarial basis for every two years. Non-life insurers should estimate their unearned premiums at 10 to 100 per cent of net premiums, the percentage depending on the line of insurance. There is no provision regarding estimation of IBNR claims, but non-life insurers are not allowed to discount their outstanding claims.

The regulator allows non-life insurers to place up to 50 per cent of their reinsurance risks overseas. Nevertheless, private insurers tend to cede 100 per cent of their reinsurance risks to Shadharan Bima Corporation. The 1990 amendment permits life insurers to cede up to 100 per cent of their life reinsurance risks to overseas reinsurers.

Republic of India

The government finally formulated the Insurance Regulatory and Development Authority (IRDA) Act in 1999, and in 2000 established the IRDA as a new regulatory body of the insurance industry. More importantly, introduction of this law has resulted in the reopening of the insurance market to the private sector and foreign insurers.

Market access regulation

A newly licensed company must raise an initial paid-up capital of at minimum 1 billion rupees (or 100 crore) for direct insurance business, or 2 billion rupees for reinsurance business. Each license is valid for three years, and can be renewed, for three years per renewal, upon the holder's meeting the licensing requirements at the time of renewal. The authority does not permit insurers to conduct life and non-life businesses concurrently. The new insurer must be an Indian company, which can be jointly created with local partners or with a foreign partner. The foreign partner must be an insurance company, and can own up to 26 per cent of the joint venture equity. The local partner can be any qualified entity (e.g., a bank).

Solvency regulation

Every registered insurer must maintain a required minimum solvency margin, the excess of the value of its assets over the amount of its liabilities. In the case of a life insurer, its margin

© 2002 The International Association for the Study of Insurance Economics.

must be the greatest of (1) 500 million rupees (1 billion rupees for the life reinsurer), (2) a sum not exceeding 5 per cent of the mathematical reserves for direct business and reinsurance assumed (without deducting reinsurance ceded), or (3) a sum not exceeding 1 per cent of the aggregate coverage (sum at risk) for the policies they have underwritten. For non-life insurers, the minimum solvency margin is the greatest of (1) 500 million rupees (1 billion rupees for non-life reinsurers), (2) a sum equivalent to 20 per cent of premium income, net of reinsurance, or (3) a sum equivalent to 30 per cent of incurred losses, net of reinsurance claims.

Financial and accounting regulation

The IRDA (Investment) Regulations of 2000 and its amendment in 2001 detail how insurers and reinsurers should apportion their invested assets to the designated investment areas. These regulations also list approved investments for certain types of assets using "exposure/prudential norms" guidelines. Reinsurers in India are subject to the guidelines for non-life business until a separate guideline for reinsurers becomes available. In short, insurers must invest their assets in securities that are actively traded in any stock exchange in India. The IRDA does not allow any unapproved investments, and all investments must be made in securities rated "very strong" by a reputed and independent rating agency.

The IRDA has imposed specific rules related to asset and liability valuation. It publishes liability valuation schedules for life and non-life insurance business. Non-life insurers are required to estimate and maintain three types of reserves: an unearned premium reserve (also known as reserve for unexpired risks), a reserve for outstanding claims, and a reserve for claims incurred but not reported.

Market conduct regulation

The IRDA has introduced regulations applying to pricing as well as terms and conditions in insurance contracts. In particular, despite the fact that fewer lines of insurance will be subject to pricing regulation, the IRDA, through the Tariff Advisory Committee, is still expected to exert influence on premium rates as well as on terms and conditions of non-life insurance policies.

There are three specific rules related to reinsurance transactions. Insurers are advised to maintain the maximum possible retention commensurate with their individual strength and business volume. Each insurer must cede a stipulated percentage, currently 20 per cent, of the amount of insurance for policies in India to the Indian reinsurer before it places part of the risk with another reinsurer. Finally, the Indian reinsurer, the General Insurance Corporation of India, assists all non-life insurers to organize domestic pools for reinsurance surpluses in fire, marine hull, and other classes.

All insurers must devote a certain percentage of their insurance business to rural and social sectors. In the case of a new insurer, 5 per cent of the total life insurance business during the first year of operation must be from such sectors. This target percentage rises to 15 per cent after five years of operation. In non-life insurance, new insurers must generate 2 per cent during the first year of operation and 3 per cent during the second year of their gross premium income from crop, cattle and farm equipment protection insurance. This rises to 5 per cent after three years in operation.

© 2002 The International Association for the Study of Insurance Economics.

Kingdom of Nepal

The Insurance Board, empowered by the Insurance Act of 1992 and the Insurance Rules of 1993, regulates and supervises the Nepalese insurance industry. The board created the Tariff Advisory Board in 1996, which is responsible primarily for ratemaking.

Market access regulation

The applicant of insurance business must send its application to the Insurance Board that may later seek approval of the application from the government. The application must include, among other things, a business plan and, in the case of a foreign applicant, a certificate from the insurance authority in its country of domicile. If the application is for life insurance business, the applicant must obtain prior approval from the Nepalese Government. The Insurance Board requires from the new insurer a minimum paid-up capital of 100 million Nepalese rupees for non-life insurance business, or 250 million rupees for life insurance business. Although it may not strongly encourage it, the government, through its Insurance Board, allows foreign investment up to 100 per cent of the paid-up capital of an insurance company.

Solvency regulation

All insurers must meet the minimum solvency margin requirement set by the Insurance Rules of 1993. For this, an insurer must deposit a minimum of 50 per cent of direct earned premiums into a statutory reserve fund. It must set aside 115 per cent of the outstanding claim reserve as a technical reserve, and transfer 50 per cent of profit to this reserve until the fund amount becomes equal to the paid-up capital. In the case of the life insurer, its assets must be greater than its liabilities.

Islamic Republic of Pakistan

The Securities and Exchange Commission of Pakistan (SECP), created in 1999, is the regulatory authority of the financial services sector, including the insurance industry, in the country. The government also introduced the Insurance Ordinance in 2000.[9]

Market access regulation

Life insurers must meet the minimum paid-up capital requirement of 100 million rupees by 31 December 2002, followed by a higher requirement, at least 150 million rupees, by 31 December 2004. Non-life insurers are required to meet the minimum paid-up capital of 50 million rupees by 31 December 2002, followed by a higher requirement, at least 80 million rupees, by 31 December 2004. Until 31 December 2002, existing insurers are subject to the minimum paid-up capital requirement of 30 million rupees for life business, or 40 million rupees for non-life business. The SECP may restrict an insurer, whether in life or non-life business, from operating one or more lines of business within the licensed class. No insurers in Pakistan are allowed to do business in both life and non-life classes.

Insurers must deposit their statutory funds with the State Bank of Pakistan, either in cash or in approved securities estimated at market value on the day of deposit, or partly in cash and

---

[9] This ordinance does not apply to insurance business carried out by the federal or provincial government.

© 2002 The International Association for the Study of Insurance Economics.

partly in approved securities. The minimum deposit amount for the fund is currently the greater of (1) 10 million rupees, or (2) 10 per cent of the insurer's paid-up capital. The Insurance Ordinance of 2000, on one hand, gives the SECP the power to change this amount or rule at its discretion. On the other hand, the regulator may, subject to achievement of levels of solvency as required by the ordinance, abolish this requirement, i.e., reduce the required minimum amount to zero.

Solvency regulation

A life insurer must at all times maintain in its shareholders' fund a surplus of admissible assets in Pakistan over liabilities in Pakistan of not less than the required minimum amount. Life insurers are currently allowed to meet the minimum, 35 million rupees, set by the repealed Insurance Act, but are required to meet the new minimum of 75 million rupees by 31 December 2004.

In the case of a non-life insurer, the insurer must at all times have admissible assets in Pakistan in excess of its liabilities in Pakistan of an amount greater than, or being equal to, the minimum solvency requirement. The minimum amount must be the greatest of (1) an amount set by the SECP, (2) a percentage of its premiums, net of reinsurance, earned during the preceding 12 months, or (3) a percentage of the sum of its unearned premium reserve and loss reserves, net of reinsurance, up to 50 per cent of the gross figure. A few exceptions to this requirement exist.

Other regulation

The SECP not only has the power to regulate terms and conditions of insurance policies. It also has the power to regulate premium rates or to set tariff rates. Direct insurers may cede their risks to overseas reinsurers but after placing a compulsory treaty cession to the Pakistan Insurance Corporation. The percentage of this compulsory cession, subject to the maximum amount of insurance, was reduced to 15 per cent as of 1 January 2001 from the previous 20 per cent. The government plans to further reduce the percentage to 10 per cent from 1 January 2003, and to 0 per cent from 1 January 2004.

Democratic Socialist Republic of Sri Lanka

Sri Lanka introduced the Regulation of Insurance Industry Act (No. 43), which became effective on 1 March 2001. And, it created the Insurance Board of Sri Lanka in March 2001 as the new regulatory authority of the insurance industry.

Market access regulation

An applicant of non-life insurance business is asked to raise a minimum paid-up capital of 50 million rupees. If, however, it raises an initial capital of at least 25 million rupees but less than the required minimum, the applicant may still get a limited license that permits it to write premiums up to three times of its initial capital. This rule also applies to an applicant of life insurance business except that the minimum paid-up capital is 25 million rupees for a full license and a minimum of 15 million rupees for a limited license. The government now allows foreign investment in local insurance companies up to 90 per cent of the equity.

© 2002 The International Association for the Study of Insurance Economics.

Other regulation

Under the new law, life and non-life insurers are required to invest 30 per cent and 20 per cent, respectively, of their reserve funds (and probably capital, too) in government securities. The Insurance Board has the authority to determine the institutions or investment instruments in which insurers must invest the balance of their reserves (and capital). This is a departure from the previously required investment of 50 per cent of life business reserves and 30 per cent of non-life insurance business reserves in government securities, and the balance in approved securities as defined in the Insurance Act (Ekanayake, 1999).

The Insurance Board is empowered to set minimum and maximum rates that licensed insurers can charge for their fire, motor and workers' compensation insurance products. Non-life insurers are no longer subject to compulsory reinsurance cession to the National Insurance Corporation, which is now privatized. They are also free from prior approval requirement for reinsurance arrangements. However, the Insurance Board reserves its right to examine reinsurance arrangements, and, if necessary, prohibit an insurer from engaging in arrangements with certain reinsurers.

3. Summary and conclusions

The growth potential of an insurance market can be measured using changes in insurance consumption and the insurance penetration ratio. Figure 1, for example, shows insurance consumption and insurance penetration ratios for selected Asian countries from 1996 to 2000. For comparison purposes, the same information for OECD member countries and G7 countries, both in aggregate, are added to the figure. This figure shows that the insurance penetration ratio has grown much faster in Hong Kong, Malaysia and Taiwan than in OECD or

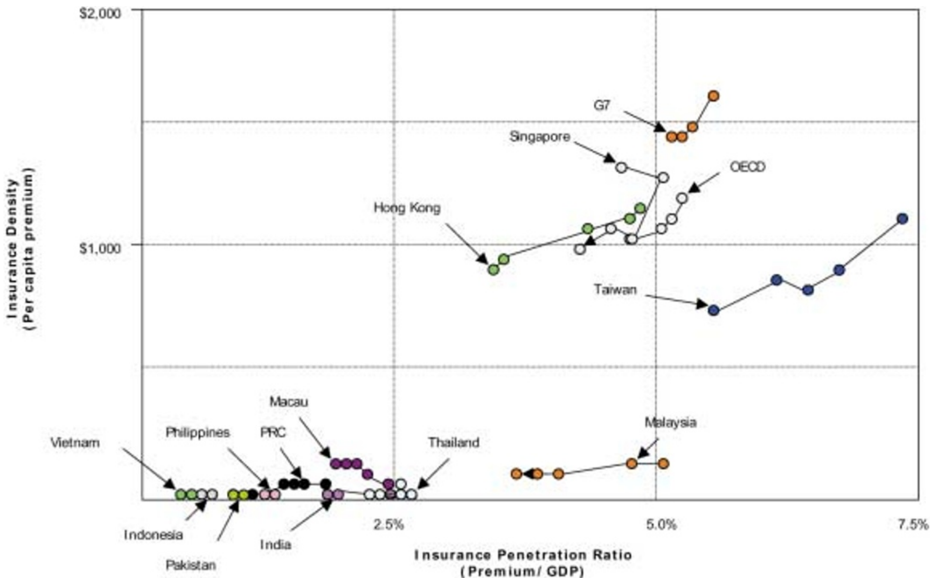

Figure 1: Insurance penetration and density ratios (1996–2000)

© 2002 The International Association for the Study of Insurance Economics.

G7 countries during the period of study. The data for other Asian countries indicate rather small changes over the same period.

Figure 1, however, fails to capture the real magnitude of market changes in Asia. This is corrected in Figure 2 that illustrates rates of changes in insurance consumption and insurance penetration ratios in selected Asian countries.[10] The results for OECD member and G7 countries, which commonly have saturated insurance markets, show that their rates of change in insurance consumption are clustered around 1.5 to 4.5 per cent with an exception for 1998–1999. The rates of change in insurance penetration ratios are also clustered around 0.5 to 4.5 per cent for these benchmark countries. In contrast, Asian markets were more dynamic, and insurance consumption as well as insurance penetration ratios changed more widely from one year to the next. Hong Kong, India, the PRC, Taiwan and Vietnam show that their insurance markets outperformed those of OECD or G7 countries for most periods, while others did not enjoy the positive and fast growth rates that they did before the 1997 Asian economic crisis.

A market can also be examined with respect to competitiveness in the market. This can be done using the Herfindahl index: the sum of the square of market shares of all insurers. Another proxy measure is the firm concentration ratio: the higher the ratio, the more large insurers are likely to carry out anti-competitive activities in the market, *ceteris peribus*.

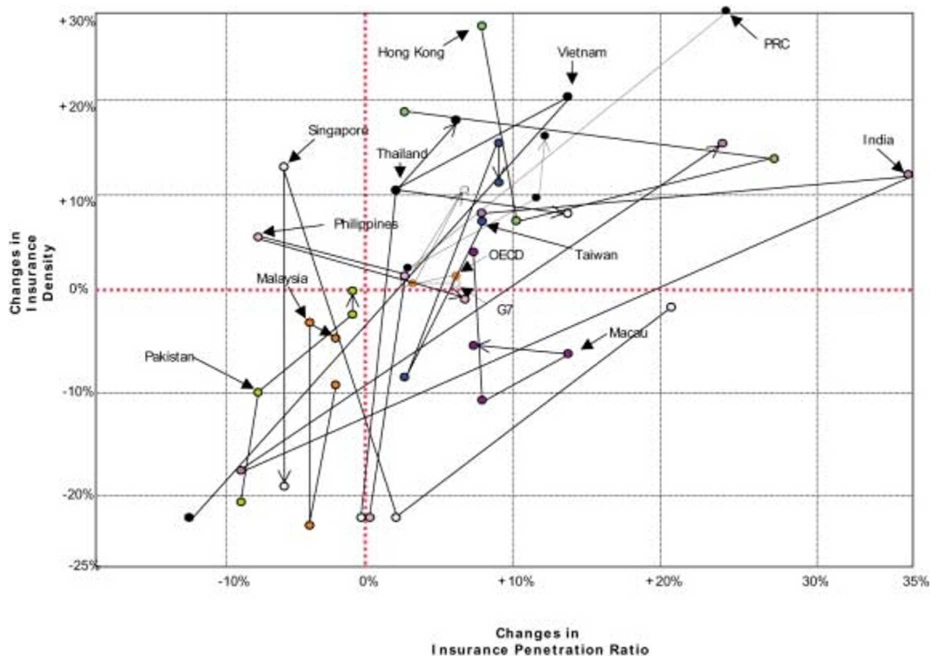

Figure 2: Rates of change in insurance penetration and density ratios (1997–1999)

[10] The rates of change for 1999–2000 are not included in this figure due to differences in data collection methods.

© 2002 The International Association for the Study of Insurance Economics.

Table 1:
Summary of key changes in insurance regulation and supervision in Asia

Country		**Key changes**
Greater China		
P. R. China	1998	The China Insurance Regulatory Commission (CIRC) created.
	2002	China becomes a WTO member.
Macau	2000	The Monetary Authority of Macau (AMCM) begins to supervise monetary and financial services industry operations in the country.
Taiwan	2001	The Financial Supervisory Board Law and the Financial Holding Company Law introduced. Insurance Law amended.
	2002	Taiwan becomes a WTO member.
ASEAN Member Countries		
Cambodia	2000	The National Assembly passes the country's first insurance law.
Malaysia	2001	Bank Negara Malaysia (BNM) introduces a financial sector reform plan in part to promote consolidation of insurers through mergers and acquisitions. Higher minimum capital and solvency margins imposed.
Myanmar	1996	The Insurance Supervisory Board formed.
Philippines	1996	Foreign firms allowed 100 per cent ownership of local insurers and reinsurers.
Singapore	1999	The Insurance Intermediaries Act introduced (to be replaced by the Financial Advisors Act of 2001, which has yet to become effective).
	2000	The Insurance Law amended. Monetary Authority of Singapore permitted 100 per cent foreign ownership of locally incorporated insurers.
Thailand	1998	28 new insurers licensed. Higher minimum capital and solvency margins imposed.
Vietnam	1999	Foreign insurers admitted.
	2000	The country's first Insurance Law introduced.
Indian Ocean		
Bangladesh	1999	30 new firms licensed for insurance business.
India	1999	The Insurance Regulatory and Development Authority (IRDA) created. Foreign joint-venture ownership of local firms permitted.
	2000	A series of new regulations begins to be introduced.
Pakistan	1999	The Securities and Exchange Commission of Pakistan (SECP) formed.
	2000	The Insurance Ordinance introduced.

continued overleaf

© 2002 The International Association for the Study of Insurance Economics.

Table 1: (continued)

Country		Key changes
Sri Lanka	2001	The Regulation of Insurance Industry Act (No. 43) becomes effective. The Insurance Board of Sri Lanka created new regulator of the insurance industry.

Table 3 presents Herfindahl indices and five-firm concentration ratios in selected Asian countries based on information for 1999 or later. Hong Kong, which maintains a liberal regulatory environment, shows that its insurance market is relatively competitive, and no insurer would be large enough to exercise control over other insurers in the market. In contrast, Singapore, another country with a developed insurance market, shows a high Herfindahl index and an extremely high five-firm concentration ratio for the life insurance market. Similar results are found for Thailand. The findings for the PRC and Vietnam indicate that their insurance markets are highly concentrated, and a few insurers probably control the market. Although not included in this analysis, many other emerging Asian markets that recently abandoned state-run insurance operations (e.g., India) or that are less developed (e.g., Myanmar and Nepal) would reveal high firm concentration ratios or Herfindahl indices. Finally, when compared to life insurance markets, non-life insurance markets in most Asian countries, except for the PRC and Vietnam, show a relatively low Herfindahl index or a firm concentration ratio. A market with a high Herfindahl index along with a high firm concentration ratio may need some corrective measures in place to minimize, if not eliminate, any anti-competitive threats.

When compared to a tightly regulated market, an open insurance market, on one hand, can make more insurance products affordable and available to an increasing number of individuals and businesses, subsequently increasing the contribution of the insurance industry to the local economy. On the other hand, an open environment can make the market more vulnerable to market distortion and insurer failure. Hence, it seems critically important at this juncture to investigate whether these emerging Asian markets are ready for competition and what additional measures the local governments should implement for the healthy growth of the markets.

Requisites for the development of a competitive market

Market access

With the exception of Cambodia, which still maintains a state monopoly in the insurance market, all countries have finally privatized the industry, at least in part, especially the direct insurance sector. Other countries with a private-sector-led market have also opened up access to the local insurance market. In contrast, access to the reinsurance market is closed in most countries, and restriction on foreign ownership of local insurance business remains an issue in several countries. China currently limits such ownership to 51 per cent, although this restriction will be removed within two years from its accession to the WTO, or by yearend 2004. Indonesia allows up to 80 per cent foreign ownership of newly incorporated joint ventures, but this percentage must be reduced to 49 per cent in 20 years. The maximum

© 2002 The International Association for the Study of Insurance Economics.

Table 2:
Summary of market access regulation

Country (currency)	**Foreign ownership**	**Minimum capital requirement**	**Other**
Greater China			
P.R. China (RMB)	51 per cent restriction (to be removed by 2004)	200 million RMB for a restricted area 500 million RMB for nationwide operation	Special admission criteria rules for foreign applicants; composite insurance business not permitted
Hong Kong (HK$)	None	$10 million for each class $20 million for composite business	Lower capital requirement for captive operation
Macau (patacas)	None	30 million for life business 15 million for non-life business 150 million for life reinsurance 100 million for non-life reinsurance	Lower capital requirement for branch operation
Taiwan (NT$)	None	$2 billion	Lower capital requirement for other branch operation than by foreign mutual firms; composite insurance business not permitted
ASEAN Member Countries			
Brunei (B$)	None	$1 billion	Composite business by *takaful* insurers only
Cambodia (new riel)	?	?	Only one insurer, Caminco, operates in the country
Indonesia (rupiah)	Initial 80 per cent restriction to be reduced to 49 per cent over 20 years	2 billion for domestic life business 4.5 billion for joint-venture life business 3 billion for domestic non-life business 10 billion for domestic reinsurers 30 billion for other reinsurers	

continued overleaf

© 2002 The International Association for the Study of Insurance Economics.

© 2002 The International Association for the Study of Insurance Economics.

Table 2:
(continued)

Country (currency)	Foreign ownership	Minimum capital requirement	Other
Laos (new kip)	?	?	Only one joint venture, AGL, operates in the country
Malaysia (ringgit)	Foreign branch operation no longer permitted	100 million (from 2001)	Special rules for insurance and captive operations in Labuan
Myanmar (kyat)	?	20 million for life business 200 million for non-life business	Only two local composite insurers operate in the country
Philippines (peso)	None	75 million for domestic direct business 300 million for foreign direct business 150 million for reinsurance business 500 million for foreign reinsurance business	Special admission criteria rules for foreign applicants
Singapore (S$)	None (from March 2000)	25 million for direct or reinsurance business	Lower capital requirement for special (limited) license and for captive operation
Thailand (baht)	25 per cent restriction (to be increased to 49 per cent)	500 million for life business 300 million for non-life business	
Vietnam (dong)	Restricted	140 billion for Vietnamese life firms US$10 million for foreign life firms 70 billion for Vietnamese non-life firms US$5 million for foreign non-life firms	Branch operation may not be permitted; composite insurance business not permitted
Indian Ocean Countries			
Bangladesh (taka)	Closed to foreign firms	75 million for life business 150 million for non-life business	Conditional licensure may be granted for firms with a temporarily lower capital than required

continued overleaf

India (rupee)	26 per cent restriction	1 billion for direct business 2 billion for reinsurance business	Composite insurance business not permitted
Nepal (rupee)	May allow up to 100 per cent ownership	250 million for life business 100 for non-life business	Composite insurance business not permitted
Pakistan (rupee)	Closed to foreign firms	100 million for life business (to be increased to 150 million by 2004) 50 million for non-life business (to be increased to 80 million by 2004)	Composite insurance business not permitted
Sri Lanka (rupee)	90 per cent restriction	25 million for life business 50 million for life business	Conditional licenses may be granted for firms with a temporarily lower capital than required

© 2002 The International Association for the Study of Insurance Economics.

Table 3:
Market concentration in selected emerging Asian markets

	Number of firms*		Herfindahl index		Five-firm concentration ratio	
	Life	**Non-life**	**Life**	**Non-life**	**Life**	**Non-life**
Hong Kong	140	45	963	251	61.5%	24.8%
Indonesia	62	107	1317	381	66.2%	34.3%
Macau	9	15	2019	78.82%		
Malaysia	18	53	1495	352	72.6%	30.3%
Philippines	40	110	1615	335	76.0%	31.6%
PR China	47		5180	6398	99.1%	98.1%
Singapore	14	50	2380	391	91.2%	32.6%
Taiwan	33	29	1771	805	78.47%	47.63%
Thailand	73	25	2975	462	90.2%	37.4%
Vietnam	4	10	10000	3908	100%	94.8%

* Based on the latest information available; otherwise based on 1999 data.
Source: Swiss Re (2001), Office of the Insurance Commissioner of Hong Kong, 1999; Insurance Department Annual Report (Taiwan); Macau Insurance Report 2000.

foreign ownership allowed is 26 per cent in India, 25 per cent currently in Thailand, and 90 per cent in Sri Lanka. Unfair rules regarding initial capital requirements imposed on foreign applicants are also found in Indonesia and Vietnam.

These differences in capital requirements and limited access to the local market should be minimized, if not eliminated. Otherwise, such a limit can reduce insurer underwriting and large-line capacity. This limit, when coupled with a lack of management control by foreign partners, can discourage further foreign direct investment in the country, especially in its financial services sector. Making available reinsurance arrangements freely, but from financially sound reinsurers, is another issue in this regard. In sum, all insurers in a local market must additionally be subject to unequivocal national treatment.

Solvency regulation

Most governments have solvency margin guidelines: some are detailed, and others are unsophisticated. The margins are commonly set as a function of the insurer's size of business measured by premiums, claims, or both. There are additional regulatory, albeit crude, measures that control the amount of insurance coverage, per risk or in aggregate of all risks that each insurer assumes, based on the size of the insurer's capital (policyholders' surplus). Nevertheless, the existing solvency margin guidelines fail to fully reflect differences in size among insurers operating in the same class, in risk and investment portfolios of individual insurers, in reinsurance arrangements, and in other insurance business-related risks. This can result in inadequate capital buffers for those insurers that expand rapidly, operate in volatile lines of insurance business, or take excess risks in their investment and other activities. It also appears that most countries do not have well articulated methods enabling insurers to estimate their unearned premium reserves and loss liabilities, IBNR claims in particular.

To better address these issues, the existing formulae need modification to reflect not only

© 2002 The International Association for the Study of Insurance Economics.

underwriting risk and pricing risk, but also asset risk, credit risk and other business-related risks. As local insurers can offer insurance protection regionally and internationally, the regulator should also consider foreign exchange risk in formulating solvency margins. An alternative approach could be to adopt risk-based capital models, which Indonesia, Malaysia, Singapore and Taiwan have or plan to introduce, or more advanced solvency margin formulae of international standards.

Focus on expost regulatory measures

In the new regulatory environment where *ex post* regulatory measures are increasingly emphasized, the importance of prudent financial and accounting regulation cannot be underestimated. Without prudence in such regulation, the regulator/supervisor may not be able to monitor in time and effectively any signs indicating market distortion or financial difficulty of an insurer. A useful tool for this purpose is the regular gathering and analysis of material financial and accounting information from licensed insurers. Another useful tool is prescribing guidelines that allow reasonable, but somewhat conservative, valuation of insurers' assets and liabilities. Permitting insurers to invest their assets in a wide array of investment areas that are commensurate with their liability exposures is equally important.

Development of the financial services sector

With an exception of Brunei and Hong Kong, regulators in the region commonly prescribe the areas of investment as well as the percentage of the assets that insurers are permitted to invest. Some countries require insurers to invest a certain percentage of their capital, including premiums, to government securities or designated sectors of the economy. In particular, the Malaysian regulator makes it compulsory, unless it has granted an exemption, for insurers to maintain at least 30 per cent of their investment in *Bumiputra* shares. Insurers in India are required to invest a certain percentage of their business in social and rural sectors as well as in economic infrastructure. Those stringent investment guidelines, especially when they limit insurers' investment to the local economy, may not only hinder insurers in the region from investing prudently consistent with their risk portfolios and business philosophy but may also affect the cost of insurance that their policyholders end up paying for.

A related issue is whether the local financial services sector, especially the capital market, is mature enough to offer a wide range of investment opportunities for insurers.[11] Without the presence of a financially sound and strong capital market, insurers face difficulty in diversifying their investment risks. Nor can they closely relate the duration, risk and investment return of their assets to those of their liabilities. As such, limited investment choices on top of stringent investment guidelines can be an impediment to further development of the local insurance market.

Human resources development

With an exception of a few countries, there is probably a widespread shortage of qualified insurance professionals – actuaries, underwriters, claims adjusters, investment

[11] This may not be of great concern to Hong Kong, Macau, Singapore and Taiwan.

© 2002 The International Association for the Study of Insurance Economics.

specialists and market specialists – in emerging Asian countries. The causes of this shortage are manyfold: decades-long national monopolies, use of tariff rating, lack of new product developments, or a shortage of training institutes or universities offering insurance programs.[12] As the insurance industry develops, it certainly needs more local expertise in insurance business. These needs cannot be met solely via skills-oriented training programs only. The insurance industry, as well as the regulatory authority, is undoubtedly in need of well educated professionals specializing in insurance and actuarial science. A long-term solution would be to promote collegiate insurance and actuarial science education and to encourage academic research in insurance and related areas. The convergence of financial services industries also suggests that such expertise should additionally include other areas of the financial services sector: banking and investment services.

Public education

Insurance is probably the most effective low cost and systematic risk management mechanism that protects individuals and businesses from scores of risks. It is also an effective mechanism to preserve or accumulate wealth for holders of life insurance and their beneficiaries. These benefits of insurance and its superiority, in many respects, over other investment mechanisms as a wealth protection mechanism might not be widely, or correctly, known to the peoples and firms in a number of emerging Asian countries. Regulators and insurance players need to put more emphasis on educating the general public about insurance. Such a campaign will be effective and result in a rise in insurance consumption when the market is served by prudent, operationally and financially sound insurers, and when rigorous regulatory mechanisms are in place to protect policyholders' interests. Policyholders should also be discouraged from exercising adverse selection against insurers or committing fraud.

Conclusions

The insurance markets in Asia are now in the process of privatization, liberalization and deregulation. This process toward free trade in insurance services is not only in line with the reform of the economy, including other sectors in the financial services industry, but also in line with those governments' efforts to meet international best practices in insurance regulation and supervision. Of course, the entire lines of insurance may not be deregulated for one reason or another, and a perfectly competitive market would only be observed in theory. However, the regulator must minimize, unless it can eliminate, any unnecessary constraints in the insurance market, while it closely monitors all the activities in the market, especially those related to financial stability of insurers, for the development of a sound insurance industry.

A deregulated and liberalized market environment pressurizes insurers to increase their efficiency and be more competitive, while such a competition does not necessarily lead to market distortion. Insurers in a competitive market will focus their *modus operandi* on developing expertise in all areas of insurance operations, thus being able to offer a wide array of insurance products. When the market is also liberalized, even if not fully, foreign capitals and expertise will flow in to the local market and all the participants in the market can receive the benefits resulting from the scale- and scope-economy effects of insurance operations.

---

[12] See Kwon (1999a, 1999b) for a discussion about the current status of collegiate insurance and actuarial science education as well as training institutes in Asia.

© 2002 The International Association for the Study of Insurance Economics.

To create a more efficient market and a competitive market environment, all interested parties must be actively involved. The regulators should impose only those rules and regulations that promote fair competition within the market, and must not attempt to use the insurance industry as a simple means of supporting another industry or purely as a source of capital for economic development. Insurers in the countries should be financially sound, technically competent in insurance matters, and must remain prudent in management and operation. The people as well as public and private entities in those countries must enhance their understanding of the benefits of insurance, and demand and consume insurance products that meet their insurance needs. Another prerequisite would be political stability in some of the countries. When these prerequisites are met, the insurance industry can further benefit the local economies in those countries and eventually help the economies to continue to advance.

SELECTED REFERENCES

AUTORIDADE MONETARIA de MACAU, 2001, *Compensation and Valuation of Assets Constituting the Patrimony of Pension Funds of 2001*. AMCM Notice No. 006/2001, Macau: AMCM.

AUTORIDADE MONETARIA de MACAU (AMCM), 2001, *AMCM/GEE Newsbrief.* Macau: Autoridade Monetaria de Macau, 15 November.

AUTORIDADE MONETARIA de MACAU, 2002, *Report on the Insurer Activity 2000*. Macau: AMCM, 20 February. [*http://www.amcm.gov.mo*].

BANK NEGARA MALAYSIA, 2000, *1999 Insurance Annual Report*. Kuala Lumpur.

BUREAU OF MONETARY AFFAIRS, 2002, *The Financial Systems in the Republic of China*, Taipei: Ministry of Finance (15 February) *http://www.boma.gov.tw/english/efsroc.htm*.

CHUA, P.S., 1999, "An Overview of the Insurance Industry in Brunei Darussalam", *Insurance Regulation and Supervision in Asia*. Paris: OECD.

DEPARTMENT OF INSURANCE, 1999, *1999 Annual Report*. Beijing: Ministry of Finance.

EKANAYAKE, G.D.C., 1999, "Investment Regulation: The Regulatory Framework in Sri Lanka", *Insurance Regulation and Supervision in Asia*. Paris: OECD.

GRIMMETT, J.J., 2000, "China's Accession to the World Trade Organization: Legal Issues", *Congressional Research Service Reports*, Washington, D.C., 2 June.

INS COMMUNICATIONS, 2000, *ASEAN Insurance Directory.* Singapore.

Insurance Act of 2000. Singapore: Monetary Authority of Singapore.

Insurance Companies Ordinance (Chapter 41) of Hong Kong, 1983. Hong Kong.

The Insurance Companies (Margin of Solvency) Regulation of 1995. Hong Kong: Office of the Commissioner of Insurance.

Insurance Law of 2001. Taipei: Taiwan.

Insurance Regulations of 1999. Singapore: Monetary Authority of Singapore.

Insurance Regulatory and Development Authority Act of 1999. India.

Insurance Regulatory and Development Authority (Investment) Regulations of 2000. India, August 2000.

Insurance Regulatory and Development Authority (Preparation of Financial Statements and Auditor's Report of Insurance Companies) Regulation of 2000, India, August 2000.

ISHII, H., 1999, "Insurance Regulation and Supervision in Asia", *Insurance Regulation and Supervision in Asia*. Paris: OECD.

KWON, W.J., 1999, "Collegiate Insurance and Actuarial Science Education in Asia", *1999 American Risk and Insurance Association meeting* (10–12 August), Vancouver.

KWON, W.J., 1999, "Insurance Training Programs in Asia Insurance Industry", *The Third Annual Conference Proceedings of the Asia-Pacific Risk and Insurance Association* (19–21 July), Hong Kong.

KWON, W.J., 2001, *Toward Free Trade in Services: the ASEAN Insurance Market*. Washington, D.C.: International Insurance Foundation.

KWON, W.J., 2002, *An Analysis of WTO Policy Impact on Insurance Regulation and Supervision in Greater China – People's Republic of China, Hong Kong, Macau, and Taiwan*. Washington, D.C.: International Insurance Foundation (forthcoming).

KWON, W.J., 2002, *The Insurance Markets of South Asia – Bangladesh, India, Nepal, Pakistan, and Sri Lanka*. Washington, D.C.: International Insurance Foundation.

© 2002 The International Association for the Study of Insurance Economics.

KWON, W.J. and MAYSAMI, R., 1999, "An Analysis of Islamic Takaful Insurance – A Cooperative Insurance Mechanism", *Journal of Insurance Regulation* (Winter), pp. 109–32.
LE, Q.B., 0000, "Vietnam's Newly Developing Insurance Market", *Insurance Regulation and Supervision in Asia*. Paris: OECD.
Macau Insurance Ordinance of 1997. Decree-Law No. 27/97/M, Macau.
MINISTRY OF FINANCE (LAOS), 1999, "Country Note: Laos", *Insurance Regulation and Supervision in Asia*. Paris: OECD.
MINISTRY OF FINANCE (THAILAND), 2000. *Additional Measures to Strengthen the Economic and Social Foundation for Long-term Sustainable Growth.* Bangkok: No. 98/2000, 31 October.
New Insurance Company Regulations of 2000. Beijing: China Insurance Regulatory Commission.
PRICEWATERHOUSECOOPERS, 1999, *Asia Pacific Insurance Handbook.* Melbourne.
PRIVATIZATION COMMISSION, 2001, [*http://www.bangladeshonline.com/pb*]. Dhaka: Ministry of Finance.
Regulations of the People's Republic of China on Administration of Foreign-invested Insurance Companies, 2001. Beijing: People's Republic of China.
Regulations on Granting Special Approval and Administration of Foreign Insurance Companies (amended in May 2001). Beijing: Ministry of Finance.
STATISTICS AND CENSUS SERVICE, 2002, *Key Economic Indicators*. Macau: Statistics and Census Service of Macau, 2 January [*http://www.dsec.gov.mo/*].
SWISS RE, 2000, "Emerging Market: The Insurance Industry in the Face of Globalization", *Sigma*, Zurich: Swiss Re.
SWISS RE, 2001, "Insurance Markets in Asia: Sanguine Outlook Despite Short-term Uncertainties", *Sigma,* Zurich: Swiss Re.
SWISS RE, 2001, "World Insurance in 2000", *Sigma,* Zurich: Swiss Re.
WORLD TRADE ORGANIZATION, 2001, *Report of the Working Party on the Accession of China*. Washington, D.C.: WTO, 1 October.
WORLD TRADE ORGANIZATION, 2001, "Report of the Working Party on the Accession of the Separate Customs Territory of Taiwan, Penghu, Kinmen and Matsu: Addendum", WTO Ministerial Conference. Doha: WTO, 9–13 November.

© 2002 The International Association for the Study of Insurance Economics.