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## Legislative disadvantages and their impact on the liberalization scope of insurance industry in Kosovo

### Abstract

This topic reflects an authorial overview regarding the complexity of the insurance market in Kosovo. As a result of the past, the particular political circumstances, the delayed social transition, poor economical growth, absence of sufficient legal state functioning, in particular the insurance market, and insurances as institutions themselves, are characterized with a poor development and with evident problems in the country. The number of companies operating in this market and the number of provided products, either compulsory or voluntary, is very small, and not only because of the impact of the above mentioned circumstances, but also because of insufficient awareness of citizens for the benefit from insurances, lack of governmental programs and the considerable lack of the legislative basis. Therefore, it is expected that very soon the compulsory insurance subject in Kosovo will be regulated by a more advanced law. Under this new legal basis the issues of institutional supervision of insurances should be regulated. Beside the legislative regulation of this field in compliance with the necessary international standards, it is necessary to create also an institutional, relatively liberal control system. How this system will be controlled depends exactly on the socio-economical growth level of the country, the demand the society makes to this protection system, and the willingness of the insurance market to provide such a service.

**Keywords:** insurance, legislation, regulation, convention, policy, premium, risk.

### Introduction

The modern world is filled with unforeseen occurrences. Risk, the word used to express the probability of a loss, continuously threatens individuals, associations, and society in general. The risk is insecurity, or an unforeseen possibility for a misfortune which causes losses and shows in an economic damage. The main questions to be raised for insurances today are whether there is a genuine insurance market in Kosovo, what is its market function, and which is the legal basis of its action, how much and how are the citizens and businesses informed on the existence of this insurance market? Indeed, these are some of the essential questions to be raised and which expect an answer of who bears the responsibility to support this field in order to provide a proper and detailed research, which is really lacking in Kosovo. Of course, first it is expected from relevant governmental bodies, insurance associations, and stakeholders. However, at the current level based on available data and knowledge we can conclude one answer: there is an unsecure market in this country but it is not clear how much is its accurate extend. Currently, if you ask an ordinary citizen what insurances are, you can get basically two different answers: insurances paid to get the pension, and the second – car insurance! Thus, there is no clear concept for insurances. At any moment social, pension insurances, etc. could be confused with other insurances. This results from the lack of educating of population with the concept and importance of insurances. If we think that on the legal basis for insurances there is not a very convenient legislation and measures are being taken by the gov-

ernment in order to complete it and to approximate it with the European standards to increase state control on insurance activities, that is not what is happening. Until now it has not been worked in the aspect of increasing the awareness of citizens to be included in the insurance market. To some point this can be justified with the circumstances that this condition is a result that except the high rate of unemployment in Kosovo, its population has a concerning percentage of poverty. However, this should not mean that this industry should flounder, in the contrary at least the citizens should be aware and responsible for the benefit insurances provide in poverty conditions as well. Concrete examples from many developed western countries, and also from developing countries show the willingness of governments to undertake limited enforcing measures to make the population aware for the insurance market. Now this phenomenon is so frequent in these countries and it is even difficult to find an aspect of their daily life, where the insurance activity is not considered. Starting from this, it is proved that in this aspect their own country should be the promoter and investor of civic consciousness first of all, same as in western countries. This should not be understood that everything should be done only by the state, which is competent to issue laws and enforcing decisions to obligate the citizens and businesses to insure their wealth. The institutional state task should be focused to rational moment dealing with the increase of civic awareness so that everyone would understand that it is a necessity to undertake to insure everything related to their daily activity, their wealth. The examples are more than evident and confirm that even the West itself having achieved so far, managed it by the force of law. At the very end, democracy is execution of law.

## 1. Trends in the insurance industry in Kosovo

Even after 12 years from the beginning of the activities of the modern insurance industry it is again affirmed that this market is not developed yet. The main indicator by no doubt is the low rate of insurances entering into business as well as to individuals and Kosovo families. On average, an individual pays less than 10 Euros per year for compulsory insurance and even less for voluntary insurance. On other words, Kosovo has the lowest report in Europe, GDP with the collected premiums within a year. Moreover, the structure of collected premiums (the report within sold products) indicates that most part of market continues to be predominated from compulsory insurances (compulsory insurances of motor vehicles and the payment of salaries dedicated for the pension fund). If we add the car insurance called Casco and the limit insurance (compulsory car insurance with foreign license plates entering the territory of Kosovo) then we could say that the insurance market is dominated by motor vehicle insurance of over 90%<sup>1</sup>. Simply said, Kosovo insurance market is too small not only compared with the neighboring countries, but also with the potential possibilities the local economy has itself. With all socio-economical difficulties in this low growth level of insurance industry, there have been identified also issues dealing with the fact that insurances are an industry which should be supported in: complex legal infrastructure; sophisticated technical models of assessing and administrating risks; recognition of techniques for transferring the risk in the international reinsurance market; a minimal culture of public awareness.

Today in the post-modern world insurances are considered as one of the most adjusted industries in the legislative aspect. This due to the fact that they are an industry in the interest of the public, where companies collect money to take over compulsory or vulnerably liabilities for the wide public. Each collection of every insurance company “creates” multiple liability for the clients in case of accidents or natural disasters. Except licensing conditions of companies to practice their activity (which are adjusted by insurance and reinsurance law), for every product or risk category there are stipulated regulations which companies are obligated to respect. On the other hand, the minimal payment ability, the capital and reserves (the available fund for payment of damages to happen in the future) are stipulated in

details in the law and in other sublegal acts. In the conditions of Kosovo, most of the cases the legal system in the part of sublegal acts is not compatible with the European insurance system. The legal framework should strictly regulate, control, and assess each element of insurance activities. It is sufficient to mention that for each modification in the statute of an insurance company, regardless how unimportant it is, the approval has to be received first from the Supervision Institution of the Central Bank in Kosovo (CBK). The new laws for the organization and operation of this supervision authority, those for licensing agents, the directive of treating damages, or the regulations for payment ability and calculation of technical provisions are a part of the legal picture which regulates the insurance market.

Beside the regulation and completion of the legislative basis, it is an urgency to improve the control of market deviation, and at the same time unjustified decrease of prices beyond the real assessment of risk. Each contract entering into market, except the legal aspect, where liabilities and the rights of companies and clients are foreseen, has “to invest” a preliminary technical work related to the calculation of premium, the assessment of the kind and rate of risk, evaluation, maintenance of the company (how much the company can burden itself and how much it has to transfer in reinsurance)<sup>2</sup>. This process is necessary especially when dealing with property insurance. In big developed markets recognized models of mathematical statistics are implemented in order to identify and assess the tendency of unexpected natural events, but also for other kinds of risks such as traffic accidents. In the last analysis what is requested to know is what average probability could an event happen (frequency of an accident), average size of financial losses and the maximum probability of losses of an event. Under the basis of these conclusions the appropriate tariff system is built to create a sufficient amount of incomes to afford damages, reserves and administrative expenses.

## 2. Lack of insurance culture and civic awareness

It is a world known fact that world countries are classified according to the rate of economical growth in: developed countries, developing countries and third world countries. The insurance industry is one of the main indicators for the rate of economical growth in a country and the presence of informal occurrences there. In developed countries (unlike Kosovo) there is a consolidated education of the population for the necessity of insurances as a result of the development

<sup>1</sup> UNMIK regulation – #2001/25 on licensing, supervision and regulation of insurance companies and insurance mediators with the purpose to implement article 6 of UNMIK regulation #2001/25, the Central Bank Board of the Republic of Kosovo in the meeting held on September 25, 2008, approved as follows: Rule 3 on the modification of regulation for compulsory insurance of auto-responsibility.

<sup>2</sup> UNMIK regulation – #2001/25 on licensing, supervision and regulation of insurance companies and insurance mediators dt. October 5, 2001, article 57 to 63.

of private property institution and the monetary interest. Whereas in our country, starting from the current conditions, one of the main tasks of insurance companies results to be the activity to increase population awareness for the necessity for insurances, this way to reveal the potentials of a “sleepy” or “possible” market. In countries with economical growth substantially dominate incomes from life and property insurances, in comparison with vehicle insurances. This medal has its second side which is interpreted and results that even in the field, where insurance companies invest, the collected incomes from life insurances are much higher than in developing countries. Long-run investments are noticed mainly through the stock market and securities, whereas insurance associations from the financial status have equaled with banks of the second level and operate similar to consumer credits. As far as the insurance premium is concerned, if we consider it as a complex mathematical phenomenon, it is evaluated that it is an indicator of premium-claim indicator (which for the conditions of Kosovo market is positive) and the price of provided services in case of damage, and the price of private property. This makes us think that the level of insurance prices in Kosovo coincides with the level of insurance market itself, meaning the sold and purchased services in our economies.

### 3. The liberalization process of insurance market in Kosovo – a challenge, opportunity or necessity?

The liberalization of insurance market was by no doubt one of the priorities of the Central Bank in Kosovo due to clear goals of the country, headed towards the harmonization of legislation itself with European directives. Another reason was the necessity to follow trends in the insurance industry in the region and wider. All these changes incited the authorities in Kosovo to take concrete steps towards the liberalization of insurance market to some extent. Characteristics of a liberal logic is considered to be the liberalization process of TPL because the insurance industry is assumed to be an open system-market without any restriction in the structure of company ownership and no other restrictions which in one way or another would favor local companies compared with foreign companies<sup>1</sup>. Under the current local legislative basis in the insurance industry there can operate foreign operators as well, whereas the ownership structure within a company has no

restriction in relation to internal or external owners. As far as investments are concerned, they are liberalized because every company can invest depending on policies and the philosophy of its investment. Restrictions in relation to the reinsurer are related with the level of bearing the risk and not on the compulsory insurance in the local market as in different countries, where they impose local and foreign companies to insure to a particular level in the local reinsurance company<sup>2</sup>.

Realistically, only in 2007 it was started to think about the liberalization of autoliability market because based on the social circumstances in our country this product was and still remains to be compulsory. During that year it was managed to create a professional commission – experts who together with the Central Bank and the insurance companies in order to compile a project for the liberalization of insurance market in the country. The specifics of Kosovo then were very different from others<sup>3</sup>. From the beginning we have stressed that the entire insurance market in Kosovo was of 92% from autoliability. The existence of such a project for liberalization was accompanied with different concerns<sup>4</sup> which by the impact of circumstances were oriented towards an approach which was based on the dilemma for the rate of controlled or totally free liberalization. The said project provided determined choices or methods which would be solved for the liberalization rate of insurance market. However, exactly on this stage of market liberalization price and competition would depend. It is interesting to mention the fact that with the compilation of this strategy it would be managed to focus the awareness of companies in issuing products based on insurance conditions, but it turned out not to be the case, however the process created the condition of reducing the prices in the average of 24-25%. Out of this situation it turned out that no company in this market competition could benefit a wider space in the market than

<sup>2</sup> For more see UNMIK regulation – #2001/25 on licensing, supervision and regulation of insurance companies and insurance mediators dt. October 5, 2001.

<sup>3</sup> Insurance association in Kosovo (IAK) was established in April of 2002, based on the agreement of Insurance Companies which were licensed to practice their insurance activity in Kosovo. The association was established with the purpose to improve the Insurance Industry in Kosovo, to support in the market stability in the Insurance market, to provide education for the staff of Insurance Companies, and to increase human resources in general, in the insurance aspect. Another priority of the Association are also the organization of different national and international seminars and conferences and to inform the public for the insurance subject in general. For more, see: <http://www.iak-ks.com/shqip/aboutus.html>.

<sup>4</sup> The responsibility of the commission not to determine strategy mechanisms which would impact and allow to occur the Greece case of liberalization, where 30 insurance companies buncrupted, the Guarantee Fund buncrupted which with big loans barely survived the crisis, in Germany a part of small companies buncrupted, and had over 2 billion losses.

<sup>1</sup> Currently, Kosovo is a member of the Green Chart System since Article 4.2 of the Council Constitution of Bureaux requests that a Bureaux, which aims to become a member, should be an internationally recognized country and to be admitted as a member of the United Nation Organization. Therefore, due to the lack of the green chart drivers, who want to enter Kosovo, should be provided with border insurance to get the car autoinsurance with foreign plates, which means cover of all damages caused to the third party.

before. It results that TPL premium is reduced for the first quarter of year 2009 for 16 %, and there was a payment reduction for damages to 17%. This condition has not even been analyzed in details for premiums and damages. Regardless, if data is available or not from anyone, there is the necessity to create a new data base with accurate information for damage backgrounds. According to this and other recommendations we can prepare the material, based on which it would be possible to get conclusions regarding the necessity and the liberalization rate of the insurance market in the country.

Modernization of the legislation in the insurance scope in Kosovo, a condition for liberalization of the insurance field in Kosovo.

In Kosovo there is lack of the law on general insurances which at the very last should be the source and basis of the entire primary and secondary legislation in the insurance scope. Consequently, the UNMIK regulation 2001/25 is still into force, which in the current aspect regulates this significant life segment as how insurance companies function as a whole. Realistically said the time, dynamic and the necessity for country growth is not the proper one at all. Due to this there is the unquestionably social necessity to urgently issue, complete and change the current legal base and transform it to a compatible legislation with European standards. Issue of such systematic laws, sub-legal acts, either general or particular ones, to regulate the scope of mandatory or vulnerable insurances would clearly regulate the issue of determining the field, activity and competences of insurance institutions. Special emphasis should be given to the institutional regulator in the supervision quality for functional regulation of the insurance market, and the same time it would impact to create proper standards on free competition basis and in achieving an optimal liberalization rate. At least according to our perceiving, most of the stakeholders which have focused their housing activities in insurances have convinced themselves that if the liberalization of insurance market occurs, the state will resigns from tariffs and will lose its role as a regulator. This is not only a totally wrong perceiving, but it is also totally impossible. Regardless of the determined rate of liberalization in the insurance market, due to the role and the significance the Regulatory Institution has in this scope, it is burdened with the task and activity for the basis of law which are considered as very rigorous that initially to ask for a reliability capital system, to request accurate information on the reserves of companies, to update and review this data, calculation of damage reserves, etc. Since legally the Guarantee Fund is not nominated here yet, and with the

role it has this mechanism not only should regulate clearly and accurately, but also should have an efficient function<sup>1</sup>. Lack of such a fund increases the insecurity of the entire insurance system due to the fact that in case of bankruptcy of an insurance company difficulties would be created in compensating individual damages from the fund. In the event that the holder of a company policy of insurance which may eventually go into liquidation is unable to meet the requirements of the liquidation proceedings due to lack of asset liquidation which do not belong to company, then these items would have be compensated by the Guarantee Fund and therefore all companies will not have serious loss<sup>2</sup>. Precisely for this reason the definition of the role of the regulator in these moments should be strictly regulated by law, clear in content but also effective implementation. In the circumstances of the global financial crisis it is often found that excessive liberalization of the financial crisis has brought this issue, so the dilemma will remain. In relation to these opinions we think that insurance at least can be found guilty of this crisis, quite the contrary. Misuse of justice, bad management and disregard of the professional rules are the causes of the crisis. Therefore, the issue of insurance law in our country must address two dimensions. Firstly, because of the current situation it should be allowed to all classes of insurance premiums for voluntary are liberalized, so that insurance companies, based on estimates and professional rules, freely identify it, and the regulator to make the approval or not – their approval<sup>3</sup>. Secondly, the part which is dedicated to compulsory insurance legislation should ensure that liberalization of the insurance market will adjust in a more controlled and relatively liberalized. The insurance needs to regulate a process, where the risk manager needs to take into account all the risk management process in order to be successful in this process. Therefore, the legal regulation of this issue essentially the risk management process will be reached as to maximize

<sup>1</sup> Currently this issue is regulated with regulation 9 on description of requests for reserves of insurance companies, based on compliance with the authorisation given according to article 17b of UNMIK regulation #2001/24 dated October 1, 2001 on the modification of regulation #1999/20 on Bank Authority and Payments of Kosovo and the article 3.3 of UNMIK regulation #2001/25 dated October 5, 2001 on the licensing, supervision and regulations of companies and insurance intermediaries, with the purpose to execute article 28 of UNMIK regulation #2001/25.

<sup>2</sup> Article 30 on the validity and amount of damages to shareholders and creditors in liquidation, pursuant to article 17b UNMIK regulation #2001/24, dated October 1, 2001 to regulate the UNMIK regulation #1999/20, on the Banking and Payments Authority of Kosovo, and Article 3.3 of UNMIK regulation #2001/25 of October 5, 2001 on the licensing, supervision and regulations of insurance companies and insurance intermediaries, in order to implement article 74 of UNMIK regulation #2001/25

<sup>3</sup> Law on competition #2004/36 – the purpose of this law to ensure the development of a stable market economy in Kosovo by prohibiting actions that restrict, suppress or distort competition.

on space and on the results of which we control. On the other hand, we will reach to minimize those spaces on the results, of which they have absolutely no control. Above we concluded that the insurance market in Kosovo is a modest market and focused on compulsory insurance. However the volume of voluntary insurance poses a health insurance market, which the country is still at low levels. It follows that the legislation should have enough flexibility to enable and stimulate growth of voluntary insurance. Additionally, growth and development of marketing plans to improve the image of insurance companies, brings a greater recognition of the services, providing a wider range of services internally, as well as a better service towards the customers outside Kosovo.

#### **4. Liberalization of compulsory insurances needs to be controlled**

The liberalization process in some countries has marked a progress; some of them are at the early stage, some – in the middle. Precisely, for these reasons the liberalization has to be viewed as an evolution process, which always requires to be improved and requires options for an easy passing and harmonization with the European directives. In fact, when talking about full liberalization, within the legislative framework, according to some assessments by legal experts of countries that have a more developed insurance market in the region, this has to result with the full adoption of more than 50 laws, that need to set forth, regulate and follow up the insurance business. As such we shall not take under consideration only the law on audit of insurance companies or law on compulsory insurance, but an entire complex set of laws that have to be adjusted in the most appropriate manner, that will enable an opportunity and full access of capital of companies that come from abroad. After regulating this legislative part, opportunities and circumstances will be enabled for a liberalization of non-compulsory insurances that need to be fully liberalized and the compulsory ones partially liberalized. In the property insurance market, the possibility of permanently lowering the general premium has to be taken into account. In the area of compulsory insurance the approach has to be changed and this has to be undertaken as soon as possible in our country, because disobeying or incompleteness of certain legal regulations contributes for certain operators in market to create a chaotic by violating the rules or profession of insurances. The price for auto insurance liability in the Republic of Kosovo is defined and is under the control of governmental authority, respectively the commission, which deals with adequate pricing of insurance that responds to the height of the damage. The main target of the Central Bank of Kosovo should focus on preparing new laws on insurance in accordance with European Union directives respecting the particulars of Kosovo. Also,

with the help of World Bank experts the law on compulsory insurances has to be drafted.

#### **Conclusions and recommendations**

No one has doubts that our country needs to create an accountable market of insurance industry through creating basic conditions for its functioning. In order to implement, this it is necessary to enhance the legal level respectively the legislation in terms of insurance liberalization. With the Constitution of Republic of Kosovo we have determined that we are for a free and open market economy, therefore it is fully understandable that insurance industry has to move forward in this direction. The existing insurance legislative framework, regulation #2001/25, which at the present time although not suitable for the time was based or supported by best international legal practices and it is close to European Union Directives as far as the organization of insurance companies is concerned. Insofar, this regulation has created an opened insurance market, provided a freedom of entry for insurers within the insurance market of Kosovo, it has provided freedom of movement of assets, freedom of distribution of dividends, has ensured an equal position to all operators, regardless of their country, origin, whether they are locals or international. However, now we are convinced that completion of legislative framework being aware of the extent of the liberalization of this segment is not easy to claim that it is an urgent need. Firstly, the competition authority professionally would not allow the insurance market to be dominated and controlled in violation with principles of the market economy. Regardless of the difficulties and risks the liberalization process must not be set aside in terms of this area. To the liberalization process a special regime has to be set up. Any state intervention in this area has not to be viewed as a denial of initiative or demand for realization of liberalization, but in these relations there has to be an alignment and accordance. This market, respectively this industry in Kosovo, marked an evident success during this period although not satisfactory. The reasons why the insurance companies exist are their costumers and coverage of their risks. Therefore, the appropriate treatment of the costumers and their right to be compensated for the damage incurred, for cases that are insured for, requires a quality approach and treatment. Thus, the increase of the competition means dynamism, development, responsibility and transparency. The meaning consists on autoaccountability, which in majority of the countries throughout the world is in the edge of falling or facing with huge losses; however in Kosovo during the last four years this industrial sector remained a profitable one. No doubts, this happened because of a huge number of old vehicles that are circulating. However, today in Kosovo roads, most probably we have only 10 percent that are new vehicles changing the existing situa-

tion within this sector, because the value intends to increase. In such terms the regulator, which in this case is the relevant department of Central Bank of Kosovo, needs to further monitor solvency of technical reserve as well as damages incurred. It appears that existing legislative framework imposes a full liberalization as well as the necessity for the institutions to regulate the market and to have an adequate role and function in order to provide a survival for the existing operators. The current circumstances raise the need to have a controlled liberalization within the area of compulsory insurances, otherwise there is a possibility that all of them will be diminished. With the new approach, within the focus of the regulator it is not the market regulation, but creation of standards that ensure a fair market competition, because it is the market which regulates the position of each company separately, based on competition and quality of services and transparency. The increase of competition means development of insurance companies, development of their managerial capacities, and increase of quality of their services by putting the customer in the center of their interests.

The process of completion of the legislation in compliance with the highest international acts and standards has to be viewed as a continuous process by solving the existing problems, enabling companies not only to exist but also to make profit out of it. The insistence that Kosovo needs to work endlessly and professionally in approximation of its legislation with the one of the European Union it is more than a task and has no other alternative. In the process of completion of legislation we have to expect a commitment role and a contribution not only from the players and operators of insurance industry, Association of Insurance Companies, Government, Competition Agency, civil society and experts of this area, but also experts of World Bank, International Monetary Fund and USAID. In this direction we need to carefully go forward, basing on analysis and professional assessments. For this purpose, Central Bank of Kosovo, needs to ask for assistance from the World Bank in order to appoint missions and experts of this prominent institution, who will perform an assessment of the special aspects of this issue.

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