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THE REGULATION OF THE NIGERIAN LIFE INSURANCE INDUSTRY

1960-1988

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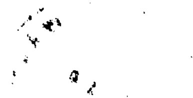

DECLARATION

No portion of this thesis has been submitted in support of an application for another degree or qualification from this University or any other Institute of Learning

ABSTRACT

This thesis examines the regulation of the Nigerian life insurance industry during the 1960-1988 period. The role and nature of regulatory policy, the extent of industry compliance with regulatory rules, and the degree to which policy formulation is subject to industry influence are examined. The changes in life industry structure, behaviour and performance are also examined in relation to the regulatory developments over the period. In this context, the effects of protectionist and other regulatory policies implemented in the industry are examined within the political economical framework of Nigeria. Three types of analytical methods are employed in the study; the historical method, the descriptive survey method and the empirical method.

Chapter one contains an introduction to the thesis and in chapters two and three, the literature on the theory of regulation, the characteristics of developing country insurance markets and the arguments in favour of and against the implementation of protectionist policy in these markets are reviewed. Chapter four places the study in context by briefly examining the political economy of Nigeria. This discussion forms the basis for the analysis of regulation and regulatory developments in chapter five. Chapter six contains the descriptive and empirical analyses of the impact of policy on market structure, behaviour and performance. In the last chapter conclusions are made and policy recommendations presented.

Although the stated objectives of regulation are a concern with the consumer and national economic interest, the results of the analyses lead to the conclusions that, among other things, (1) the development, implementation and supervision of policy has been impeded by an underresourced and understaffed regulatory agency (2) the implementation of protectionist policies in the Nigerian life market has not been successful in terms of the stated policy objectives (3) the consumer interest is in fact not being adequately protected and (4) the lack of cooperation between life offices has contributed to the industry's inability to influence regulatory policy in it's favour. It is recommended, among other things, that (1) the Government should withdraw from intensive participation in the life market and should channel it's resources towards maintaining an effective regulatory mechanism and (2) the implementation of protectionist policies in the market should be made with respect to the prevailing socio-economic and political conditions for maximum effectiveness.

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Abbreviations

CBN	Central Bank of Nigeria
GDP	Gross Domestic Product
GPI	Gross Premium Income
LOC	Life Offices Committee
₦	Naira (Nigerian Currency)
NICON	National Insurance Corporation of Nigeria
NIA	Nigeria Insurance Association
PDI	Personal Disposable Income
UNCTAD	United Nations Conference on Trade and Development

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"...Great is Thy Faithfulness"

Chapter 1

Research Background

1.1 The Motivation For the Study

A cursory review of the literature and environment of the life insurance industry in Nigeria gives rise to the preliminary conclusion that despite the phenomenal growth of the economy in the past, the industry is struggling for existence. Nigeria has a population of approximately 100 million people and it is estimated[1] that only a little over one million life assurance policies have been issued to date. In percentage terms it has been suggested that less than 5% (Kiladejo 1987,p.101) of the total population own one form of life insurance policy or other. The figure may even be considerably lower when policy surrenders and lapses as well as ownership of multiple policies are taken into consideration. In addition, most (77.3%)[2] of the life insurance underwritten in the country is in the form of group life rather than individual life business.

This figure is quite low in comparison with countries like the United Kingdom and the United States of America where about 76%[3] and 83%[4] respectively of the population own life policies. In 1986, Switzerland, the USA and Japan had the highest per capita expenditure on insurance at a time when the gap in total insurance business between the industrial and developing countries had increased substantially.[5]

The market for insurance in Africa is very small, representing 1.3% of world-wide premiums in 1981. In 1981, Nigeria's share of world-wide insurance premiums was 0.17%, a very low figure compared with the US (46%) and the UK (6.52%). It however ranked 27th out of a total of 55 developed and developing countries

1. Figure obtained from the Nigerian Insurance Year Book 1987 Edition.

2. Figure derived from the Nigeria Insurance Digest 1989.

3. Figure obtained from Insurance Facts and Figures, British Insurance Association, Various Editions.

4. Figure obtained from the Life Insurance Fact Book, Institute of Life Insurance, New York.

5. Sigma, Swiss Re No.5/May 1988.

examined, and indeed appeared to be the largest African insurance market.[6] In terms of premiums as a percentage of GNP, and premiums per capita, the country ranked 34th out of 49 (1.61%), and 47th out of 54 countries respectively. The lowest premiums per capita were recorded in life insurance business (Nabolz 1986,pp.36-45).[7] The growth of the life market in real terms was put at less than 5% in 1985.[8]

The situation does not appear to be improving. By 1986, Nigeria's share of world premiums had dropped. It was estimated at 0.02%, while the country ranked 56 out of 61 countries (6th out of at least 11 African countries) in terms of total business. Its position stood at 49 out of 61 developed and developing countries (4th out of at least 11 African countries) for life insurance business with a world share of 0.01%. Premiums per capita stood at 0.5% for life and 1.4% for non-life business, with Nigeria having the least premium per capita in all the African countries for life insurance business.[9]

1.2 The Significance of the Study

The low consumption levels of life insurance in Nigeria and the slow growth of the market are of economic and social importance for a number of reasons. Life insurance has a significant role to play in national development. Apart from its provision of protection for individuals in society, it can facilitate economic development by contributing to social stability, reducing the financial burden on the state, and serving as a source of development funds by mobilising domestic savings.[10] It's primary role is to alleviate anxiety and worry by enabling future provision to be made for retirement, old age or the death of the breadwinner in families. In addition to this, life insurance also has attendant social benefits. It encourages thrift and provision for old age/retirement and protects the individual family against the consequences of premature death, so that in the long run, the potential financial burden on the government and society, that would have arisen without it is reduced (Evans 1981;

6. With the exception of South Africa.

7. In 1985 UNCTAD launched the first statistical survey into the operations of insurers and reinsurers in developing markets the results of which were published in 1987 in UNCTAD TD/B/C.3/220 "Statistical Survey on Insurance and Reinsurance Operations in Developing Countries."

8. Figure from Sigma, Swiss Re No.5/May 1877.

9. Figures from Sigma, Swiss Re No.5/May 1988. The premiums per capita in Sigma were calculated on the basis of premiums as a percentage of GDP whereas the 1981 figures were based on GNP figures. This may account for some of the differential, but does not alter the basic argument.

Franklin and Woodhead 1980; Mehr and Cammack 1976). This occurs because life insurance encourages the savings habit among individual policyholders and as such facilitates the growth of a vibrant economy.

This is illustrated by the fact that countries like Japan, the Philippines, Singapore, Thailand and Malaysia, which have strong life insurance industries, have experienced tremendous growth in national savings and domestic investment rates which have averaged over 20% of GDP in each country. The role of financial intermediation played by life insurers is particularly important in the context of developing economies since life insurance has been proven to be an effective mobilizer of funds which can be channelled into national development activities (Greenberg 1986,pp.28-32).

The gross premium generated from the numerous relatively small premium contributions of the policyholders as a result of the life offices activities are mobilised and subsequently channelled into various sectors of the economy such as government and private securities and the granting of loans and mortgages. This intermediation is made possible because a high proportion of life funds (unlike the case with general insurance business) is available for long term investment as a result of the long term nature of life office liabilities. Thus government and other institutional borrowers can obtain financial resources for capital development more efficiently than if they had to go around borrowing numerous small sums for their capital requirements.

In the past, insurance practice in developing countries was patterned after the model of the former colonial powers who had colonised various territories. As a result, the insurance markets were open and there was limited regulation of the activities of the insurers operating in these markets. Western insurance practice was an alien activity in these countries in terms of economic structure and social organization and as such did not take into consideration the socio-economic situation of these countries. It was recognised (after the independence of these countries) that they might not experience the benefits of the institution of insurance mechanism if the insurance system did not take into consideration their socio-economic needs. Since the past and present experience of developing country insurers bears little resemblance to that of Western insurers, it was considered that the application of the Western principles and practice to the third world markets would not encourage their economic growth and development (Ripolli 1974,p.75, El-Hassan 1981,p.43). Thus efforts were made to redress this issue mostly in the form of policy recommendations by the United

10. See UNCTAD TD/B/C.3/177, 1982, "The Promotion of Life Insurance in Developing Countries".

Nations Conference on Trade and Development (UNCTAD) secretariat in Geneva. These recommendations were adopted as resolutions and their thrust was mainly on "the need to establish, encourage or consolidate national insurance institutions"[11] (Ripolli 1974,p.82). This, among other things, involved placing limitations on the operation of insurers. Thus developing country markets increasingly began to adopt restrictive measures and became "...more restrictive in outlook" (Carter and Dickinson 1978,p.3).

As a result of the UNCTAD recommendations, in many less developed countries, the investment policies of life offices are integrated with economic policies that are implemented to stimulate the development of the economy. However the successful use of the institution of insurance for facilitating economic development appears to be dependant upon the extent of regulatory control involved. Under the regulatory model, the implementation of these policies is a function of;

(1) the nature and quality of the regulations in force,

(2) the ability of the regulatory agency to enforce the regulatory provisions, and

(3) the extent to which the industry complies with the regulations (El-Hassan, 1981,p.47).

In the developing economies, it has been recognised that the support of the government in the promotion of life insurance is essential. Life insurance can achieve importance if there is an environment conducive to its growth and the attitudes and policies adopted by a government in respect of the role of life insurance and it's promotion in the country can be crucial to its success.[12] Thus in many developing economies the role of government in the insurance industry has been mainly interventionist, and this has resulted in various effects on the insurance industries concerned.[13] The interventionist measures are mainly in the form of protectionist measures imposed on domestic insurance markets and are generally geared towards;

(1) the protection of the domestic, that is, local market from foreign competition

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11. This is discussed in some more detail in chapter 3.

12. See UNCTAD TD/B/C.3/177 "The Promotion of Life Insurance in Developing Countries."

13. This aspect is fully discussed in chapter 3.

(2) the protection of consumer interests or

(3) a combination of the preceding (Skipper 1987,p.65).

UNCTAD has made policy recommendations with regard to the issue of protectionism in developing country insurance markets, and these recommendations have resulted in UNCTAD as being seen to be sympathetic to the developing country interests (Skipper, 1987,p.61). Nigeria in recent years has, to a large extent, implemented several of UNCTAD's recommendations in respect of protectionist measures related to;

(1) the limitation of the activities of foreign insurers in the local market (e.g by the use of domestication[14] policies) and

(2) the limitation of the operational activities of all insurers in the local market (e.g restrictions on the purchase of foreign reinsurance services by direct insurers).

Various justifications for the implementation of these policy measures have been given, viz, the protection of the consumers interest, and the development of a sound local insurance industry and solid local investment.[15] However, the success or otherwise of the implementation of specific policy measures geared toward the attainment of strong national markets has been called into question[16] with the developed country markets repeatedly calling for the liberalisation of trade in insurance services and the privatisation of insurance markets in the developing countries.[17] The reasons advanced for this is that many developing country markets are inefficient, undercapitalised and lack the essential expertise and infrastructure to operate domestication policies successfully.

In the light of these and related issues, this study examines the development of regulatory policies in the Nigerian life insurance industry during the period from 1960-1988. The objective is to determine the manner in which government policy in the field of insurance has influenced industry structure, conduct and performance

14. The words "domestication" and "localisation" are used interchangeably.

15. See Skipper (1987,pp.71-81) for a discussion on the rationales for protectionism in insurance.

16. A full discussion is provided in chapter 3.

17. See UNCTAD TD/B/C.3/229 "Insurance in Developing Countries: Review of Developments in 1986-1988."

during the period. The focus of the analysis is on the post-independent period (from 1960 onwards) although the historical development of the industry will be examined within the context of the study. This is because statistics in relation to insurance industry activities are available only from the 1960's. The year 1988 has been selected because industry data beyond that period are unavailable as at the time of writing. Some broad characteristics of the Nigerian economy are examined so as to describe the general environment surrounding the insurance market during this period. Thus life insurance market structure, behaviour and performance are discussed in the context of the regulatory environment and the socio-political environment.

1.3 The Statement of The Subgoals

A number of subgoals have been generated which are pursuant to the analysis.

(1) The first subgoal is to examine the role and nature of regulatory policies in the Nigerian Life insurance Industry during the period from 1960-1988. This includes an appraisal of the objectives, nature, content and scope of regulatory policy during the period, as well as the capacity of the regulatory agency, in this instance the Insurance Department, to regulate the industry. The extent of industry compliance with regulatory provisions is also examined, as well as the degree or extent to which policy formulation is subject to industry influence.

(2) The second subgoal is to examine the shifts/changes in industry structure, conduct and performance in relation to regulatory developments over the relevant period.

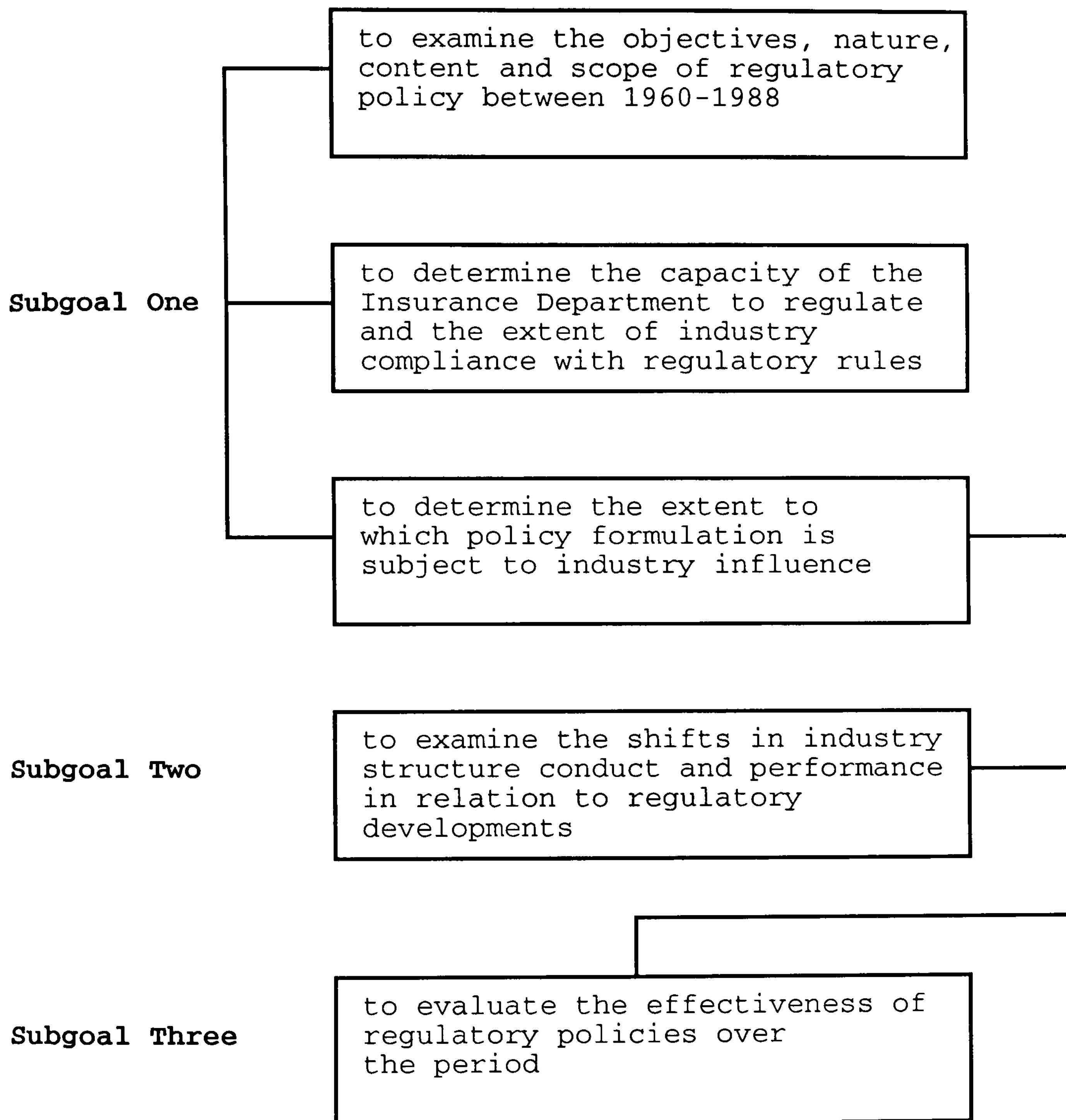
(3) The third subgoal is to evaluate the effectiveness of the regulatory policies in terms of their stated objectives over the relevant period. This is intended to lead to prescriptive recommendations as to the proper focus of future legislative action in the field of life insurance in the country.

1.4 The Delimitations

The analysis at hand suffers from a number of constraints. Although the regulatory authorities compile some data with respect to the insurance market, this data is checkered and incomplete. This is by no means peculiar to the Nigerian market. The problem of the lack of administrative data and the poor quality of available data is

Figure 1A
A Structural Representation of the Research Problem

The purpose of this study is:



Adapted from Leedy 1989

characteristic of developing countries (see Casley and Lury 1987,pp.1-14). It has been stated that politics, rather than statistics drives public policy decision making and as such the incentive to gather adequate and reliable statistics is low and so;

> "In many developing countries, despite nominal affirmations of interest, traditional administrators do not really believe in the value of...data in formulating and implementing public policy. The demand for quality data may thus be low...Politics is more often the order of the day than statistics (Bulmer 1982,pp.3-7)."

This appears to be true in the case of the Nigerian insurance market. First, in the early years, there were no legislative requirements as regards the establishment and maintenance of records by the insurance companies operating in the market. This was at the time when the market was dominated by foreign insurers, who it can be said did not care whether such records were kept in Nigeria since their activities were supervised by their parent companies abroad.

Second, even after legislative measures imposed requirements for the maintenance of records, this was done in a haphazard manner. Where the blame arises for this state of affairs is not quite clear. The insurance companies blame the supervisory authorities, and the authorities accuse the companies of not submitting records in accordance with regulatory requirements.

Third, even where the records are submitted in accordance with the legal requirement, the lack of skilled staff and computing facilities in the Insurance department preclude a competent compilation of comprehensive and accurate insurance company data.

However, in addition to the Insurance Department there are four other sources of insurance statistics which have been employed in this study. They are:

(1) The annual publications of the Nigeria Reinsurance Corporation, that is, The Nigeria Reinsurance Year Book,

(2) The Nigeria Insurance Digest, a publication of the Nigeria Insurance Association,

(3) The Annual Abstract of Statistics, published by the Federal Office of Statistics, and

(4) The Central Bank Economic and Financial Review published by the Central Bank of Nigeria.

The limitations related to the use of all of the above data sources is that some of the statistical data is inconsistent across the different government offices that compile them. For example, the statistics on premium income for the same years differ according to the data source. This is mainly because of the manner in which statistics relating to insurance activities are reported to the various bodies. The Nigerian Insurance Year Book, for example, compiles data based on returns made by insurers to both the Insurance Department and the Nigeria Reinsurance Corporation. The Nigeria Insurance Digest statistics are based on returns submitted by members of the Nigeria Insurance Association.[18] However, while these other bodies provide a good source of macro (consolidated) data in respect of industry operations, micro, that is individual company data on most aspects of insurance company operations are to be found in the Insurance Department.

The study is limited to the analysis of the activities of direct life specialist and composite offices in Nigeria.

1.5 The Data And The Treatment of The Data

The data used for this study are of three kinds, historical data, and survey data of a descriptive and analytical nature.

These data fall into two categories, primary and secondary data. The primary data utilised are the written records and accounts of past happenings and events such as the various legislative instruments and policy documents, as well as information obtained from official government and private sources (see section 1.4). The secondary data are Government and industry data bases on insurance company operations. Published studies and texts as well as unpublished studies and dissertations relevant to the subgoals have been employed for descriptive purposes.

To ensure as much as is possible, within the limitations specified above, the authenticity and validity of the evidence and data used, the sources of such

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18. The Nigeria Insurance Digest published its maiden issue in 1985, in response to the urgent need for a comprehensive database for insurance activities in the country.

information are official. In this regard "official" is not limited to Nigeria and the sources include the sources enumerated in section 1.4 above.

1.6 The Research Methodology

Three types of analytical methods are employed in the study; the historical method, the survey method and the statistical method.

The historical method is concerned with the analysis of documentary sources, and the object is

> "...to provide a means through which the researcher may deal with problems that arise from events that happened in times past and to interpret what might otherwise be considered merely as the happening of blind fortune (Leedy 1989,p.125)."

Consequently, this method is appropriate to the analysis of subgoal one, that is, the historical development of the life insurance regulation in the context of the political and socio-economic environment.

The survey method is a tool that can be used to generate information from people (respondents) who can supply information for use in examining the research problem. Surveys may be descriptive or analytical as the case may be. Descriptive surveys provide results which may be used to generate ideas and hypotheses which can subsequently be tested using statistical analysis (Allan 1991,p.179). The experience survey in particular,

> "attempts to tap the knowledge of those familiar with the general subject being investigated (Churchill 1988,p.82)."

The analytical survey method can be used to obtain quantitative data which can be tested statistically (Leedy 1989,p.89). The descriptive survey and analytic survey methods are applied to the analysis of subgoals two and three, and some of the information obtained is tested statistically as appropriate.[19]

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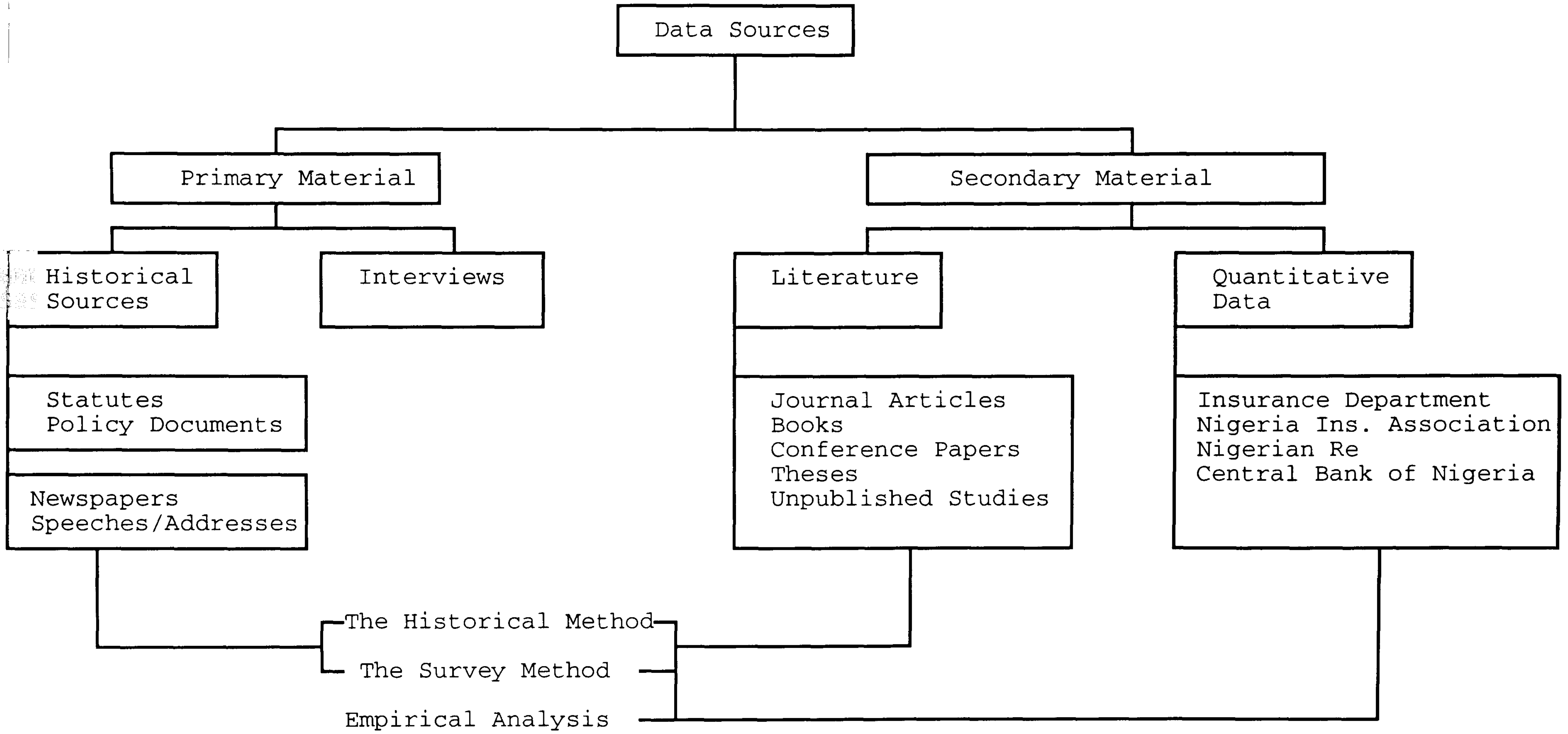
19. Methodology in relation to the analysis of statistical data is discussed extensively in chapter 6.

[illegible]ure 1B
[illegible]rces of Data and Their Mode of Analysis



During the period from May 1991 to July 1991, an experience[20] survey was conducted. Interviews were held with some insurance industry executives who were familiar with some of the issues relevant to the study. The economies of the research process necessitated a limitation of the number of executives approached. Ten insurance companies operating within the commercial centre of Lagos were approached. After repeated effort, seven companies (six direct[21] companies and one national reinsurance company) responded positively. Access to the insurance companies presented some problems. This is not unusual in the Nigerian situation. For example, in an earlier study[22] of the Nigerian insurance market, there was a marked reluctance on the part of company executives to give personal interviews. Questionnaires sent out to insurance companies were not returned. However, fortunately for the researcher, he was appointed to serve on a Government investigating committee into the industry. Consequently the companies were compelled to complete and return the questionnaires. For this study, former students and friends were used as a means of gaining access to key personnel in the insurance companies selected.

A convenience sample, rather than a random sample, was used as the basis for the selection of the companies. This was because (1) certain criteria were used as a basis for the selection of companies and (2) the use of a convenience sample reduced to some extent the problem of access to the companies.

The basis for the selection of the companies was as follows:

(1) All the companies had been operating in the market for at least ten years at the time the interviews were held.

(2) Companies with different ownership structures were selected. Out of the seven respondent companies, three were national, that is, under government ownership and control. Another three had a minimum of 40% foreign equity and one was an indigenous (domestic) company.

20. The experience survey is alternatively referred to a "key informant" survey, or qualitative interview. See Jones (1991,pp.203-214).

21. Direct insurance companies mainly underwrite direct insurance business from the insurance market and may accept reinsurance business from other insurers. Reinsurance companies specialise in underwriting reinsurance business only, and as such accept business from insurers and reinsurers only.

22. See Falegan 1991,pp.31-32.

(3) Companies with different underwriting portfolios were selected. One[23] was a specialist company, underwriting life insurance business only, while the other six[24] were composites.

The last two selection criteria were employed in an attempt to incorporate respondents who might have differing points of view with respect to some of the issues raised during the discussions. None of the companies approached was prepared to release individual company data relevant to the study. Eight senior personnel in seven of these companies were interviewed.[25] All the industry executives interviewed had spent a minimum of ten years practicing in the life insurance market.

Although a standardised[26] interview schedule was used as a guide-line, the interviews were informal. The interview format was semi-structured in the sense that although the questions in the schedule were standardised for ease of comparability of responses, the questions were open-ended rather than closed since the purpose of the interviews was mainly to solicit facts and opinions about the issues with which the study is concerned. Thus, a semi-structured informal interview process would best facilitate candid responses and also generate hitherto unknown information relevant to the study. All of the insurance company interviews were recorded on tape to encourage a free flow discussion. Although no pilot interviews were conducted because of time and financial resource constraints, because the interviews were semi-structured, this allowed for the possibility to explore any interesting issues which might be raised. The respondents were asked for permission to record the interviews on tape, and in all except one, agreed. In three cases, because of background noise, written notes were taken in addition to the tape recordings as a back-up. Respondents were asked about their views on regulation of the insurance industry in general and the life insurance industry in particular, market structure and conduct as well as their ability to comply with regulatory requirements, among other things.[27]

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23. The African Alliance Insurance Co.

24. The American International Insurance Co.; Crusader Insurance Co.; Financial Insurance Co.; Great Nigeria Insurance Co.; NICON; The Nigerian Reinsurance Co.

25. See section 5.2.2.7.

26. The respondents were asked the same questions using the same words and the questions were asked in the same order. For literature on interview techniques see, among others, Sellitz, Wrightsman and Cook (1976,pp.294-320), Churchill 1988, Allan 1991 and Jones 1991.

27. See appendix B for interview schedule used in insurance company interviews.

Two regulatory officials from the Insurance Department were also interviewed. A separate interview schedule was employed in the manner described above. However, the discussions at the Department were not recorded on audio tapes, because the respondents objected. Since the personnel interviewed were bound under the Official Secrets Act, one of them, Mr. X, apparently concerned that he might have released "sensitive" information requested anonymity.[28] This reluctance to speak had been anticipated, and in an attempt to overcome this, issues that might be considered sensitive were not broached until well into the interview after a few "tame" questions had been asked and rapport and trust established. The structure of the Insurance Department, personnel issues and the development of public policy in insurance, among other things, formed the basis of the discussions.[29]

1.7 The Thesis Structure

The study is divided into seven chapters. The literature on the theory of the regulation of markets in general and financial markets in particular is examined in chapter two. In chapter three, the characteristics of developing country insurance markets is examined and the arguments in favour and against the implementation of protectionist policies in these markets will be discussed. Chapters two and three form the conceptual basis for the study. In chapter four the political economy of Nigeria is examined briefly in order lay a foundation for the discussion of regulatory sources, their intent and content, as well as development within the context of Nigeria's socio-economic and political environment, which is undertaken in chapter five. The results of the descriptive and empirical analysis relevant to the study are presented and discussed in chapter six, while in the concluding chapter, the results are summarised and discussed in the light of the prevailing regulatory theories and arguments. In chapter seven policy recommendations are made based on the conclusions drawn from the results of the analysis.

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28. Mr X was unwilling to cooperate unless he was given the assurance that the information was to be used for purposes of research only. He in fact made the statement that "...if this (that is the information given) gets out, I will deny everything."

29. See appendix C for interview schedule.

Chapter 2

Regulation and Insurance

Introduction

In this section the concept of regulation is examined and a review of the various economic and political views as to the purposes of regulation in general and insurance regulation in particular is undertaken. The purpose is to lay a conceptual foundation for the study of insurance regulation in the Nigerian life insurance industry.

2.1 The Concept of Regulation

Regulation may be viewed as the process of subjecting an activity to some form of control. There are three aspects of the regulatory process. First, the generation or development of rules to serve as a code of conduct or behaviour. This is the nominal aspect of regulation. In addition to this, regulation also involves the monitoring or policing of behaviour. This is because regulation is meaningless unless there can be put in place a means of ensuring compliance with the rules that have been generated by monitoring the behaviour of those whose activities are subject to regulation. Then there is what can be referred to as the punitive aspect of regulation which is concerned with the punishment of non-compliance with the rules which invariably leads to the imposition of sanctions by the regulatory body.

For example, the laws of a country may be set by parliament, the function of the police is to ensure compliance with the laws, and punishment for infringement is imposed by the judiciary. In the context of insurance business, rules are generated by the appropriate governing body, compliance is ensured by the relevant supervisory authority which has been given the charge of insurance business and infringement of the rules may be dealt with by the supervisory authority and/or the courts.

Economists have long been concerned with the economic effects of regulation and a number of hypotheses regarding these effects have developed over the years. Traditionally, The Consumer Protection Hypothesis has been utilised to explain the

purpose of government intervention in markets. As it's name suggests, the basic thrust of the hypothesis is that the purpose of governmental intervention in markets is to protect the public welfare. The Producer Protection Hypothesis has been offered as an alternative explanation. It purports that the "purpose in fact" of government intervention is to protect the interests of certain groups (the producers) in the regulated industry. Posner (1971) used the phrase "purpose in fact" to "distinguish...between the reasons ascribed to regulatory laws and decisions by the legislators and regulators themselves and the reasons, whether or not anywhere avowed, that provide a consistent explanation of the actual course and consequences of regulation."

The No-effect Hypothesis (Jordan 1972,p.153) and Taxation by Regulation (Posner 1971) have also been advanced to explain the purpose of the economic regulation of industrial activities. Before the various hypotheses are examined, it is necessary to define what is meant by the word "regulation" in this context.

2.1.1 The Definition of Regulation

Regulation has been described as a process that involves "the use of governmental power to guide personal or organizational conduct" (Bernstein 1955,p.259). Although the exercise of regulatory powers is generally considered to be the prerogative of governmental bodies, it should be recognized that the performance of all regulatory activity is not necessarily restricted to government and various definitions of regulation take account of this fact.

Consider, as an example, Mitnick's (1988) work in which he offered several of what he termed "definitional perspectives" of the regulatory process. He took a broad view of regulation as the "intentional restriction of a subject's choice of activity, by an entity not directly party to or involved in that activity." This definition could encompass the efforts of say, a parent, controlling some of the activities in which his child is engaged. The definition is however restrictive because it would apparently not include the supervisory activities of, for example, the governing boards of professional organisations vis a vis the industrial activities of their members, under

the assumption that members of the board are also engaged (directly or indirectly),[1] in the activities being regulated.

Additionally, it would apparently not include a situation in which the government as the entity carrying out the regulatory activity, (the regulator) is also directly engaged in the activity being regulated. For example, the evidence in various insurance markets shows that public (government) participation in the industry may, apart from regulation, take various forms such as partnership, competition, and exclusive agency. Thus there could be a situation in which the government forms partnerships with private indigenous and/or foreign firms or individuals. The government may also run fully state owned companies which operate in direct competition with other privately owned companies. This, we shall see further on, is the situation in the Nigerian insurance market. Thus, as Mitnick points out, his definition would not apply to situations in which there is no clear cut distinction between the regulator or regulatee.

Mitnick's more restrictive definition of regulation as "the **public**[2] administrative policing of a **private** activity with respect to a rule prescribed in the public interest" excludes from the scope of the exercise of regulatory powers non-governmental institutions or entities. It also brings into focus the perceived purpose of regulatory activity-a concern with the effects of private activity on the public welfare. The nature or characteristics of both the regulatee and regulator defines the nature and sphere of regulatory activity, and this may differ from situation to situation. Mitnick (1980,p.14) expressed the various regulatory possibilities by defining what he called a "typology of regulation" in which he isolated four possibilities of regulation among public and private parties:

(1) Traditional regulation (the public regulation of private activity)

(2) Capture (the reverse of traditional regulation, that is private activity controlling the nature of public regulation)

(3) Private self-regulation (the private regulation of private parties), and

1. The nature of involvement would be indirect if, for example, a member of the board had financial interests in a particular firm.

2. Emphasis mine.

(4) Government self-regulation (the public regulation of public parties).

Insurance regulation may fall within the first three areas of activity and the broad scope of regulatory activity[3] in this area covers some of the intra-organisational and inter-organisational activities of insurance firms within the industry.

Private activity can be subject to various kinds of regulatory rules. Koch (1974,p.340) refers to the regulation of economic activity as the "comprehensive rules, instructions, procedures, and attention" that a regulatory agency imposes upon a particular industry. This definition is very broad and would include the regulation of all the significant economic variables associated with the firms' activities in a particular industry such as the regulation of products, prices, distribution and promotional arrangements.

It should be appreciated that the process of regulation is a continuing one. Regulation should not be seen in terms of static acts of control by the regulatory authority, but rather as an on-going, dynamic process (Mitnick 1988,p.8). It is the product of a dynamic process with social, political and economic determinants (Van den Berghe 1990,p.199), and it is virtually impossible to separate regulation from the general political and social setting in a society. Consequently a thorough knowledge of markets as well as their economic purpose and effects is essential to the development of an efficient system of regulation in which regulatory policy can be adapted to changes in the economic and socio-political environment (See Bernstein 1955,pp.252-257, and also Veljanovski 1988,p.7). Others share this view of the need for dynamism in the regulatory process. For example, in 1968 the Superintendent of Insurance of New York commenting on the need to keep insurance regulation responsive to current public needs and current realities within the regulated industry, stated that "Regulation is the process of bringing current values of society to bear on current practices of an essential industry, and hence regulation must seek relevance rather than permanence" (Stewart 1969,p.32).

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3. For a detailed discussion on the scope of insurance regulation, see Hellner (1963),pp.494-543.

2.2 The Theory of Regulation

Two theories have traditionally been advanced to explain the operation of the regulatory process. They are the consumer protection hypothesis (the public interest theory), which has its basis in economic theory, and the producer protection hypothesis which has been advocated by scholars in the field of economics and political science. Apart from these basic theories, over the years some scholars, dissatisfied with the traditional theories of regulation, have offered alternative theories by either modifying the traditional ones, or developing new theories. The various theories of the regulatory process are examined in the following section.

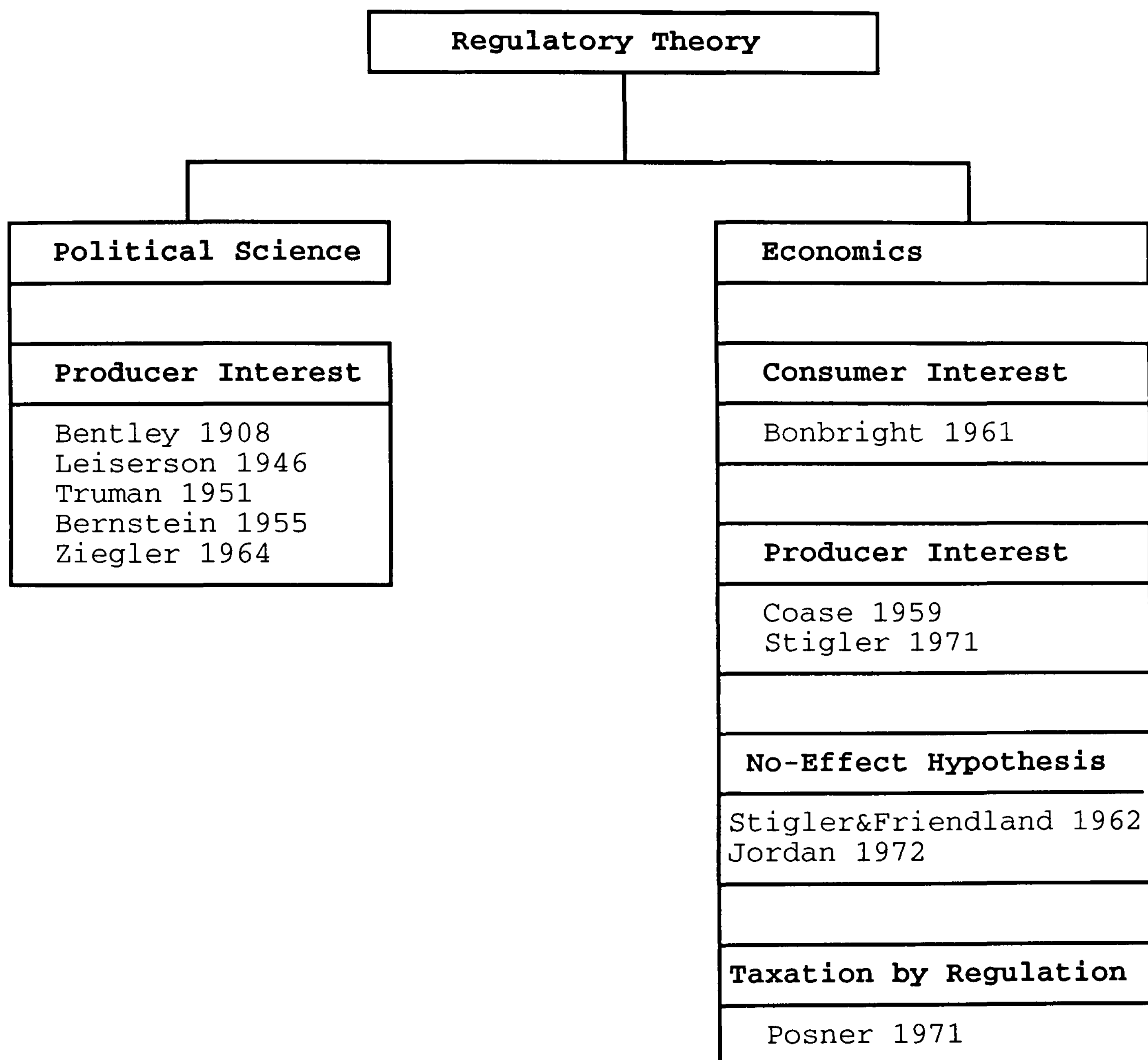
2.2.1 The Consumer Protection Hypothesis

The consumer protection hypothesis which, as the term implies, proposes that government regulation of industry is implemented to protect the interests of consumers, is the basis of what is referred to as the public interest theory. The question arises-who is the public and what is the "public interest"?.

The concept of a "business affected with the public interest" can be traced to the 17th century to Lord Chief Justice Matthew Hale, the British jurist. At that time the phrase was not used in connection with commercial enterprises. It was not until 1876, when in Munn v. Illinois (94 U.S 113) the U.S Supreme Court stated the (state) governments right to regulate "properties...with a public interest" that the phrase was applied to commercial enterprises (Mehr and Cammack 1976,p.651; Greene 1977). In 1961, in the seminal work "The Principles of Public Utility Rates" James C. Bonbright provided the basis for what came to be known as the public interest theory of regulation. He described the primary purpose of public utility regulation as the protection of consumers, defining a public utility as "any enterprise subject to regulation, including price regulation, of a type designed primarily to protect consumers," i.e "a business affected with a public interest."

The extension of the public utility concept has led to a broader definition of a business affected with a public interest. The phrase is now used in a broad sense to describe any enterprise subject to special regulation (not necessarily a public utility) of a type designed primarily to protect consumers (Bonbright 1961,pp.3-7). The term "special regulation" implies that such an enterprise would be subject to certain constraints in its operations in the market as it would of necessity have to operate in

Figure 2A
The Theory of Regulation



an environment more restrictive to its activities as compared with other businesses (Mehr and Cammack 1976,pp.651-652).

The nature of the public interest may take different forms depending upon which group or groups of people are seen as constituting the public. Although in its original sense the public is taken to mean consumers (rather than taxpayers or producers), (Bonbright 1961,p.4), the public may in actual fact largely be classes of individuals such as individual shareholders, institutional investors, or employees. The development of public interest theory was in response to the need to analyse and justify regulation and government interference in the market economy. It starts from the hypothesis that the operations of the free market economy are inefficient, this inefficiency having led to a non-optimal allocation of resources. The failure of the market may be attributed to a number of factors such as;

(1) the existence of a substantial amount of market power by a firm/firms, and

(2) uncompetitive practices such as price-discrimination among other things.[4]

The concept of public interest theory although broadly understood and applied, is largely unarticulated (Posner 1974,p.335). Its general application is however pervasive as can be seen from the fact that the professed purposes for governmental regulation of economic activity are based upon this concept. The reasons advanced for the governmental regulation of economic activity include, among other things;

(1) the need for the regulation of natural monopolies or the elimination of unreasonable monopolies,

(2) assuring fair competition,

(3) the conservation and allocation of natural resources,

(4) the promotion of an expanding economy and,

(5) the protection of consumers and investors (Koch 1974, and Mehr and Cammack 1976,p.650).

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4. For a discussion of the reasons why economic regulation may be imposed on an industry, see e.g Koch (1974) at pp.339-355.

2.2.1.1 Financial Markets and The Public Interest

Financial markets in most countries are characterised by extensive regulation. Kay (1988,pp.35-42), identifies several reasons for this:

(1) [the historical] political mistrust of the financial community by the public at large,

(2) the macroeconomic significance of financial markets and their attractiveness to the operations of sophisticated criminals,

(3) the what he terms "remarkable" vagueness of contracts, particularly insurance contracts, and

(4) asymmetry of information.[5]

Edwards (1982,p.82) argues that the one goal of overriding importance in the regulation of financial markets is "to maintain stability in financial markets and to guarantee that vicissitudes in economic activity do not undermine the economic health of nations and of the world economy". Thus other goals are of "lesser" importance since "a regulatory system that achieved these while failing to maintain financial and economic stability would clearly be a failure." Others, for example van den Berghe (1990,p.207) are also of the opinion that the stability of the financial sector is crucial to the equilibrium of the economy, since this sector is performing "a strategic buffer function".

Financial regulation has several "potential" purposes such as the protection against systemic risk i.e "the risk that some sizeable part of the system as a whole may collapse " as well as the lofty aim of investor protection. The purpose of investor protection has been defined as that of providing "regulation which should be no greater than is necessary to protect reasonable people from being made fools of."[6] The common purpose of all these defined purposes is the concern with the public welfare.

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5. Asymmetry of information is discussed further on in the paper.

6. Professor Ian Gower Cited in Veljanovski (1988) at p.7.

The theoretical foundation of the public interest theory is based in the economic theory of competitive markets. The assumptions of the theory are that, ceteris paribus, a perfectly competitive market will exhibit the following characteristics;

(1) It will be atomistic in that there will be a large number of participants in terms of buyers and sellers,

(2) Rational (profit maximising) economic behaviour will be exhibited by all participants since each of them has perfect knowledge of the market, that is, complete and accurate information of all relevant and future conditions pertaining to prices, costs, and demand in the market,

(3) Homogeneity of each sellers products and,

(4) Non-existent or insignificant barriers to entry into the market (Koch 1974,pp.15-25; Shepherd 1985).

All these conditions are obviously not fulfilled in real life markets. The financial markets is a case in point. There is a lack of complete and accurate information in these markets. This exists in the form of (1) asymmetric information between the competitors in the market place and (2) an information gap between the individual investor and the financial institutions with which he is dealing.

In insurance markets in particular, this means that most if not all the relevant information in terms of, for example, the "quality" of the insurance product relative to its price, that is needed to enable the policyholder to make the optimum, rational economic decision[7] is in the possession of the insurance company. In fact, in insurance markets, a double information gap exists because not only does the policyholder have insufficient information to make an informed decision, additionally, the insurer does not have perfect information about the nature of the individual risks presented by different policyholders (the risk exposure) with which he is dealing (Van den Berghe 1990,p.203). For example although the insurer may be able to assess with some degree of accuracy the physical hazards associated with a given risk presented by the policyholder, it would be much more difficult to measure the degree of moral or morale hazard involved.[8] These and other special features of

7. In order to make an informed, optimal decision, the policyholder should be able to make price/quality comparisons between the products of competing insurance firms as well as between the product choices available to him within a particular firm.

the insurance contract provide the explanation for its being classified as a business affected with a public interest (Mehr and Cammack 1976,pp.651-652). Thus, the existence of information asymmetry in financial markets in general "creates a potential requirement for regulation...and...lies behind the traditional regulatory posture in financial markets over the last century..." (Kay 1988,p.37).

2.2.2 The Producer Protection Hypothesis

Although some empirical evidence has been advanced in support of the public interest theory (see, for example, Moore 1961; Edwards and Edwards 1974) this view of regulation is not universally accepted by all theorists and/or empiricists. Apart from the obvious difficulties entailed in determining what constitutes the public interest[9], since different people have differing views of what constitutes the public interest, it has been argued that two apparent assumptions of the theory namely, that markets will tend to operate very inefficiently if left alone, and that there is virtually no cost associated with government regulation are not justified by the available evidence. If the assumptions were correct, it would be expected that the incidence of government intervention in markets would be positively correlated with monopolistic market structures or the presence of external costs or benefits and regulation would be a costless procedure. Posner (1974,p.336) stated that the evidence from theoretical and empirical studies conducted by economists over a period of about fifteen years did not support the assumptions. The results demonstrated that "regulation is not positively correlated with the presence of external economies or diseconomies."

Although some theorists agree that market imperfections do exist, they do not see the purpose of the regulatory process as the protection of consumer interests, but rather as a means by which powerful interests such as firms with a high percentage of market share in the regulated industry are protected as a result of what is referred to as "regulatory capture".[10] It is considered that the naive belief in the ability of the

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8. In insurance terminology, a hazard is a condition that serves to increase the probability of a loss occurring as well as it's severity when it does occur. A physical hazard is an objective characteristic such as state of health of insured, or occupation a moral hazard is a subjective characteristic which has it's basis in the mental attitudes/disposition of the insured. Morale hazards are associated with carelessness or indifference on the insureds part (see Mehr and Cammack, (1976) at pp.23-24, and also Bickelhaupt (1979) at pp.7-9.

9. See Bernstein (1955) at pp.154-163, Noll (1971) and Schumpeter (1950), in Early (1974) at p.192, who stated that "There is, first, no such thing as a uniquely determined common good that all people could agree on or be made to agree [sic] on by the force of rational argument. This is due not primarily to the fact that some people may want things other than the common good but to the much more fundamental fact that to different individuals and groups the common good is bound to mean different things."

government to correct market failures based on the assumption that government in its regulatory role is "an independent and neutral factor, able to surpass all conflicts of interest and exclusively guided by the general "public interest" is unjustified and erroneous" (Van den Berghe 1990,p.209). This is because in the long run the regulator will tend to adopt views similar to that of the regulated industry. This is because both parties are employing "similar training, similar tasks, similar data, and similar techniques" and in time will establish their values by reference to each other (Stewart 1969,p.34).

The results of some of the work done in this area appear to be inconclusive. A number of studies of some regulated industries support the view that the "purpose in fact" of regulation is not the protection of consumer welfare. For example, Coase's (1959) study of the Federal Communications Commission (FCC)[11], demonstrated that decisions taken by the FCC with respect to the licensing of broadcasting stations were not necessarily made in the public interest. Similarly, Hilton's (1966) study into the purpose, internal consistency and adequacy of the Interstate Commerce Act led to his observation that "The Act...[has]....perpetuated the problem with which it was designed to deal", that is cartelization and collusion in the railroad industry.

Huntington (1966) also studied the Interstate Commerce Commission and in his study demonstrated the way in which the ICC, in response to political demands and pressures from interest groups in the railroads, made regulatory decisions that favoured them and how the ICC gradually became dependent on the support of this segment of the transportation industry. Harris (1966) examined a specific case in which pressure groups tried to influence a regulatory agency by successfully opposing the election of a particular senator who they knew could not be subject to their political pressures and demands.

Kitch, Issacsson and Kasper (1971) investigated the regulation of taxi cabs in Chicago and came to the conclusion that among other things, political pressure in the city had ensured a limitation on the number of licensed taxi-cabs operating in the city which was not in the welfare of the consumers.

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10. Discussed further on.

11. The Federal Communications Commission is a regulatory agency charged with the supervision of the communications industry in the U.S.A.

On the other hand, there appears to be evidence that the regulation of an industry could sometimes produce mixed results, that is, the protection of both consumer welfare and the producer interest. Moore (1961) surveyed a number of regulated occupations and businesses in Chicago. His purpose was to determine whether licensing was carried out in the public interest or in order to confer monopoly power on regulated businesses and occupations. The results of the study were mixed. He found that restrictions on entry/registration which were the "least restrictive" and "least persistent" type of regulation appeared to be designed primarily in the public interest. On the other hand "non-price rationing regulations", (entry requirements that no expenditure of funds will satisfy) and the requirements of the self regulating occupations were the most restrictive and appeared to have been designed for the benefit of the practitioners in terms of preventing or reducing new entry into the professions. With regard to the licensing of occupations, his specific conclusions were that licensing raises the cost of entry into occupations because "Legislatures seem to license those occupations which it is most in the public interest to regulate and, in doing so, establish certain regulations which benefit practitioners."

Regulatory capture, that is the process by which the regulatory agency is dominated by major or powerful interest groups, within the regulated industry, is discussed extensively in the political science and economic literature. In 1971, George Stigler in his "Theory of Economic Regulation" argued that regulation of industry was not directed towards the benefit of the public interest, but that "...as a rule, regulation is acquired by the industry and is designed and operated primarily for it's benefit". He believed that the economic regulation of industry should be based on the "rational theory of political behaviour" and proposed the hypothesis that politically effective industries or occupations would seek to control entry into their industries or occupations. His thesis was that the process of the economic regulation of markets could be modelled in terms of demand/supply considerations, with the regulated industry demanding regulation and the regulatory agency supplying the desired regulation at a price which is the political support of the regulated industry. Stigler[12] has come to be considered as the founder of what is variously known as "the interest group or capture theory", "the economic theory of regulation" (Posner 1974) or the "Stiglerian" (Ippolito 1979) view of regulation.

Although Stigler's theory provoked a lot of study into the economic regulation of industry, interest group theory had however been earlier discussed in the political

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12. In 1982, Stigler won the Nobel Prize for economics, "which specifically referred to his theory of economic regulation" (Meier 1988, p.181).

science literature.[13] As far back as 1908, Arthur F. Bentley published his classical "...more often cited than read work" The Process of Government[14] which discussed the influence of interest groups over the process of administrative decision-making. This work was widely regarded as seminal, although it and the work of similar writers like Truman has been criticized as being seriously lacking in theory.[15] Posner believed that the deficiency in their work stemmed from the fact that the "theories" did not explain the reason for the effective representation of some but not other interest groups in the political process, and additionally failed to specify the conditions under which interest groups succeeded or failed to obtain regulatory policies favourable to them.

The political science literature progressively began to emphasise the special importance of a particular interest group, the firms, usually the dominant firms, in the regulated industry, and attempts were made to explain the dynamics of the regulatory process on the basis of the theory of interest groups. Bernstein (1955,pp.250-259) stated that in the context of the American environment, regulation had been actively sought by groups that were concerned that the public be protected from business practices that were inimical to the public interest. He argued that however, although there are a few instances in which an industry will demand regulation, in many cases dominant interest groups within the industry will be hostile to any form of governmental interference and may oppose it. This is because the interest groups perceive the establishment of the regulatory agency or the enactment of legislation as the case may be, as not being in the (economic) interests of the industry. Once, however, the regulatory mechanism is in force, the affected interest groups will change tactics and fight for the maintenance of the status quo, seeking for ways of influencing the decision making processes of the regulatory agency in their favour. "Reformist rather than revolutionary in orientation," they change tactics and "attempt to make public policy the instrument of their aims" (Leiserson 1946,p.296).

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13. Meier ibid., notes that Stigler's theory was largely ignored by political scientists probably because they had similar theories and they considered that this theory was not radically different from their own theories (pp.21-22).

14. Cited in the introduction to Bentley's work by Odegard, (1967) at p.xiii.

15. Posner (1974) at p.341 stated that "...Bentley and Truman and their followers,...have developed some evidence of interest groups in legislative and administrative processes, but unfortunately their work is almost entirely devoid of theory."

Economists also lent support to this view of the regulatory process. For example, Coase (1959,p.36) in his study of the FCC referred to "...the extent to which pressure is brought to bear on the Commission by politicians and businessmen...with a view to influencing it's decisions." As mentioned previously, the work of Hilton (1966) and Kitch et Al (1971) are also illustrative of the degree and nature of the pressure that can be exerted on regulatory agencies. The actual process by which the regulated industry "captures" the regulatory agency has been extensively treated in the political science literature. The interest groups engage in lobbying and similar political activities, the objective of which is to ensure that officials sympathetic to their interests, are employed in the relevant key positions in the regulatory agency (Truman 1951,pp.450-453). This they consider as being essential to protecting their interests since it is very difficult for interest groups to influence decisions if they do not have access to administrative processes (Ziegler 1964,pp.285-287). The ability of the interest groups to influence the regulatory agency is heightened by the constraints within which the agency is operating. Generally speaking, the agency may be operating within the general guidelines contained in its enabling statute and is left to its own devices in seeking to determine the exact nature of regulatory goals that are in accordance with the public interest.

Bernstein (1955,p.257) notes that regulatory agencies may experience difficulty in identifying and defining the exact nature of the public interest in a particular area of activity. An example is in the area of insurance pricing or ratemaking. In pricing insurance services, each policyholders fair share of losses and expenses is calculated. This involves the forecasting of probable claims from past losses and involves a lot of guesswork since the rates must be established before all the costs are known. There are certain principles that have to be complied with in order to scientifically calculate rates. These are, among others,

(1) Adequacy of the rates, that is the rates should be sufficient to cover losses and expenses incurred

(2) Equity in ratemaking which means that ideally all insureds should contribute to the insurance fund in proportion to their fair share of estimated losses and expenses, and

(3) Non-excessive rates, that is rates charged should not be too high (Mehr and Cammack 1976,pp.600-603).

The regulatory agency has to determine in each area of activity specified above what is in the public interest. This is not always apparent because for example, the requirement for the adequacy of rates has to be balanced with that of ensuring that the rates are not "too adequate" that is, excessive. Mehr and Cammack (1976,p.602) have noted that regulatory authorities for political reasons are more concerned with correcting excessive rates rather than with inadequate rates. This is dangerous because inadequate rates may lead to insurer insolvency. At the same time it is virtually impossible to achieve perfect equity in ratemaking and so the insurer has to class similar risks together in order to attempt to achieve some form of equity. The question is, how is the exact nature of the public interest defined with consideration to these sometimes [conflicting] goals? The regulatory agency is thus subject to pressure from interest groups within the industry who want rates as high as possible and consumer groups who want the least possible rates. All this has to be done with regard to the scientific principles that the insurance pricing process should adhere to. Thus, although the

> "...agencies must give their foremost loyalty to the public purpose entrusted to them...they cannot forget that other social groups share in that purpose and have their own notions as to how it may be best achieved....The wise administrator, therefore, keeps open the channels of information and advice between his agency and the private organizations concerned with its operation" (Leiserson 1946,p.296).

Since the dominant interest groups are by definition powerful and generally more organised than the representatives of the public interest, then the agency through continuing interaction with these interest groups will tend to adopt their particular view of the public interest (Bernstein 1955,p.154-163). Apart from this, the regulatory agency operating within a hostile environment in the form of external opposition to its establishment and existence by the regulated industry, seeks to reduce the degree of opposition by aligning its policy goals with the desires of dominant interest groups in the industry (Ziegler 1964,p.275).

Although the political science literature described how the regulated industry influenced the regulatory agency, the explanation of the behaviour of the regulators has been provided by economists. The explanation for this behaviour can be obtained from the recognition of the fact that regulators, like other human beings, are utility maximisers (Eckert 1973). They attempt to maximize some "objective function" in the decision making process (Noll 1971), and this objective function includes, among other things, the welfare of both the regulator and those that are affected by decisions taken by the regulatory agency. The welfare of the regulator includes his wealth, [illegible] conditions (Eckert 1973,p.83). The different items that comprise

the objective function of the regulator are, in varying degrees, substitutable and given the constraints under which the regulator is operating he will attempt to select among the various regulatory policy choices available to him by considering what he sees as the cost/benefits associated with each policy alternative. The decision he makes will ultimately depend on the "cost-reward" structure under which he is operating (Eckert 1973,pp.83-88).[16] The nature of the environment within which the agency is operating leads regulators to pursue what Noll refers to as "a high degree of invisibility" or alternatively "minimum Squawk" behaviour in order to reduce the hostility to which the agency may be subject (Hilton 1972,p.48). This involves to a large extent the pacification of the regulated industry (p.51). In any event, regulatory goals and policies are adjusted in line with the desires of the interest groups in the regulated industry.[17] This process inevitably leads to the exercise of "anticompetitive" behaviour and sub-optimal decision-making by the agency.[18] Regulatory capture has occurred.

Some writers like Bentley see the degree of influence over, or dominance of the regulatory agency as almost total, while others like Truman and Ziegler believe that this is not the case. Noll's view was that where several interest groups stand to gain or lose from the outcome of decisions taken by the regulatory agency in a specific issue, "the agency will tend to seek compromises among the competing...interests..." (p.17). On the other hand, Ziegler's (1964,p.iv) explicated conflict model suggests that organised interest groups represent just a portion of the whole "matrix of pressures" to which the regulatory agency is subject, and "...it is a false realism which describes governmental decision makers as passive pawns pushed and shoved about according to the whims and fancies of "powerful" pressure groups."[19] The degree of success an

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16. Eckert (1973) at pp.85-88 distinguishes between the behaviour of a bureaucratic agency and an independent regulatory commission. According to him these two regulatory systems are faced with different cost-reward structures and as such are expected in a given circumstance to make different policy decisions.

17. Noll makes two exceptions to this: (a) where the political significance of the issue is such that the decision of the regulatory agency is subject to close scrutiny by the mass media, and (b) where a "special" interest group other than the regulated industry has a major interest in the decision made by the agency.

18. Noll ibid at p.17, and also Hilton (1972), passim. Hilton was of the opinion that regulation served merely to misallocate resources and stated that "The incentives upon the commissioners [regulators] are to generate monopoly gain in one activity, either through administering a cartel or maintaining a monopoly, and then to dissipate it in uneconomic activity.".(cf Posner 1971).

19. See also Truman (1951) at p.447.

interest group will experience in its attempts to influence the regulatory process will depend on, among other things, the social status of the members of the group.[20]

2.2.3 Alternative Hypotheses

In addition to the consumer protection and producer protection hypotheses other views of the regulatory process are held. Stigler and Friedland's pioneering study into the measurement of the effects of regulation in the electric utilities industry has given rise to the "no-effect hypothesis". Stigler and Friedland (1962) studied the effects of regulation on the level of rates and returns in the industry and came to the conclusion that there were no significant regulatory effects in the market. Posner (1971) however considered that the no-effect hypothesis did not generally describe the effects of government regulation on markets. He illustrated his point with specific instances of regulated industries which had oligopolistic or competitive nonregulated market structures (the airline, railroad and freight motor carrier industries). In these cases government regulation has had an effect on the performance of the industries.

Posner (1971) also proposed a thesis he referred to as "Taxation by Regulation." His argument was that "regulation is a method of public taxation and expenditure" and based on the study of some regulated industries he came to the conclusion that the consumer protection and producer protection views did not explain the prevalence of internal subsidies in many regulated markets. He defined the internal subsidy as "...[t]he deliberate and continued provision of many services at lower rates and in larger quantities than would be offered in an unregulated competitive market , an unregulated monopolistic one." His public finance hypothesis, he believed, provided a "consistent explanation" of this and other features such as entry control among other things.

The Stiglerian hypothesis as well as the work of other "interest group" or "capture" theorists have been analysed and criticised by some researchers. For example, although Posner (1974,p.336-349) posited that the theoretical and empirical evidence did not support the public interest viewpoint he concluded that, among other things, Stigler's theory in its [then] present form was "at best a list of criteria relevant to predicting whether an industry will receive favourable legislation...[and was not]...a coherent theory yielding unambiguous and therefore testable hypotheses". He argued

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20. Bernstein (1955) and Ziegler (1964) at p.v.

that since there was inadequate empirical support for the theory, it had to be improved considerably before it could be accepted as an "adequate" theory of regulation.

Peltzman's (1976) criticism of the Stiglerian theory was less severe. One of his arguments was that although Stigler's work provided a theoretical foundation for the producer protection view of the regulatory process, it needed to take into account the fact that "...regulatory agencies will not exclusively serve a single economic interest" (p.211). He believed that regulators public policy decisions are shaped not only by the political processes involved in decision making, but also by the regulator's utility function which is conditioned by the interplay of competing interest groups that will be affected by the regulator's decisions.[21] The evidence from a study of the effects of price regulation in the automobile insurance industry lend support to this view (Ippolito 1979,p.87).

Gormley (1986) also believed that there was little evidence to support the scenario of the capture theorists. In an attempt to develop a model that could be used to predict the composition and behaviour of the various actors in the regulatory process, as well as the regulatory pathologies[22] that could be expected to emerge, he developed a categorisation of regulatory issue areas. This categorisation was dependent upon the levels of public salience and technical complexity[23] of each issue area. He concluded that it was only issue areas that were considered to be low in salience and high in complexity (for example, transportation, commerce, finance, and more relevantly, insurance), that provided an environment conducive to policymaking by a "power elite". This elite he defined as bureaucrats, professionals and business groups with the latter being the dominant interest group. Since the levels of salience and complexity varied across regulatory issue areas, and this determined the nature of regulatory politics involved, generalizations could not be made as to the nature and degree of influence of the actors involved in policymaking without taking these factors into consideration.

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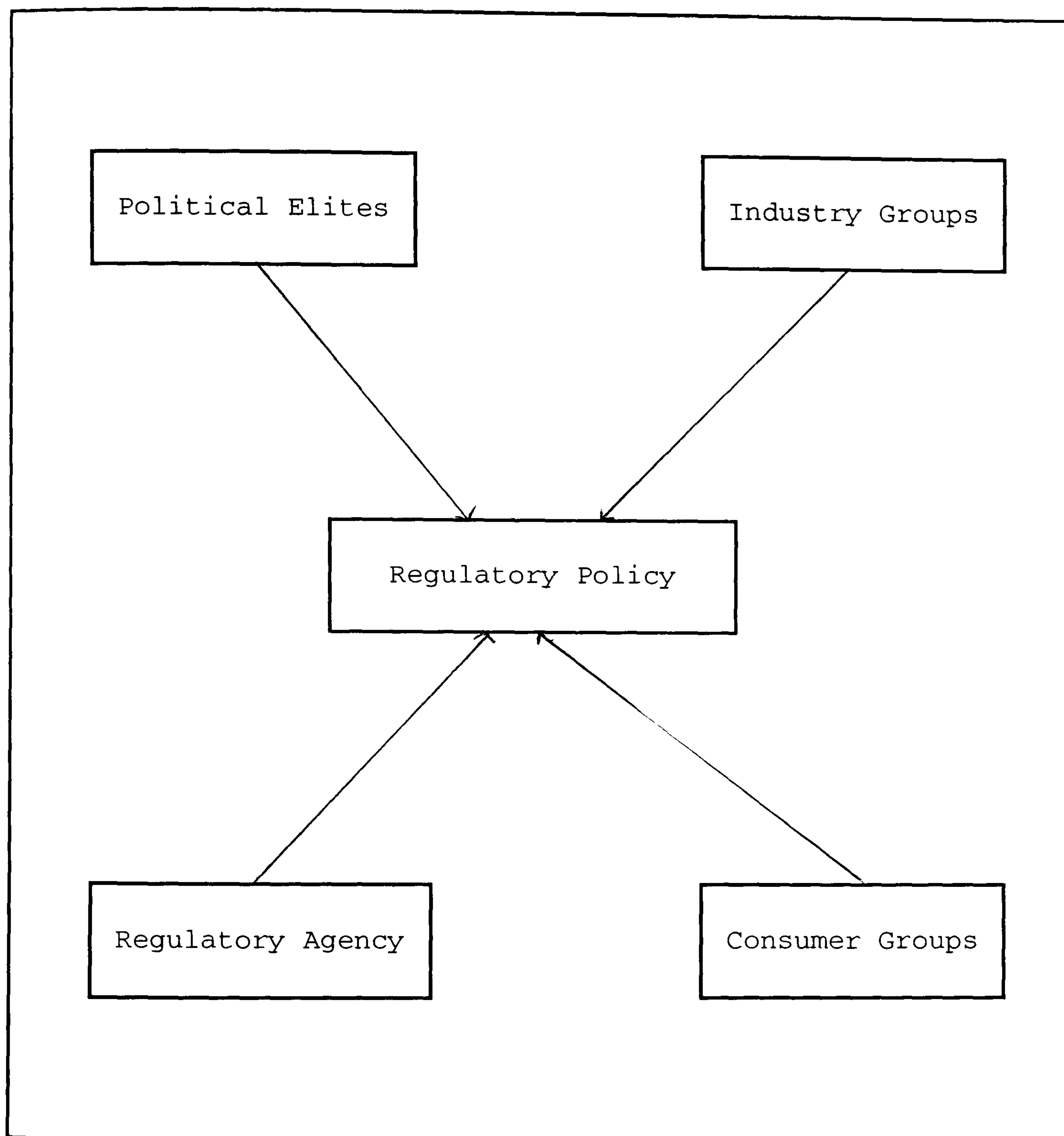
21. See also Noll (1971) at p.17 "... when several special interest groups have a stake in a regulatory matter, the agency will seek compromises among the competing powerful special interests..."

22. The nature of the regulatory politics in terms of the relative degree of influence of the various actors in the regulatory issue areas. Gormley (1985) at pp.615-617.

23. Gormley defined a highly salient issue as one that affects a large number of people in a significant way, so that the scope of conflict is broad, and a highly complex issue as one that requires specialized knowledge and training beyond the scope of generalists and laypersons.

Figure 2B
The Multi-Interest Theory of Regulation



Meier (1988,pp.18-30) critically reviewed quantitative and case study literature in the area of both economics and political science and based on the findings in these studies, came to the conclusion that "[t]he regulated industry,...,must be viewed as having multidimensional interests" (p.29).

His view was that since the various interest groups do not necessarily have the same policy goals and the policymakers are not passive actors in the regulatory process a "multi-interest" model/theory of regulatory policy could be applied to the regulatory process. This model, he believed, could be used as a basis for the analysis of, among other areas, insurance regulation.

In Meier's model, four "key actors", viz industry groups, consumer groups, the regulatory agency, and political elites, influence regulatory policy to a degree determined by (in the case of the first three) their political resources. These political resources are for example, in the case of industry groups their size and wealth (p.29).

The influence of political elites in the regulatory process he argued, was dependent upon their values as expressed by their policy goals. In Meier's framework, each set of actors in the political process will attempt to implement their respective policy goals within the resource constraints to which they are subject. Thus, the regulated industry will seek regulation that benefits it and oppose regulation that restricts it.

The various regulatory hypotheses or models that have been discussed are all intuitively appealing. Taken separately, they do not adequately explain the behaviour of both the regulated industry and the regulatory agency because they cannot be applied to all regulatory scenarios. Taken together however, as in the case of Meier's multi-interest model, they appear to explain the dynamics of the legislative decision making process.

Stigler's demand-supply theory of regulation, that the regulated industry demand regulation and the regulatory agency supplies it, in return for political favours, cannot be said to apply to all markets because it presupposes the existence of democratic decision making processes in government. The socio-political environment is taken as given, that is, a democratic system in which group dynamics can operate relatively freely. Coase (1959), Hilton (1966) and Kitch et Al (1971) also appear to make the same assumptions. It is assumed that draft bills are passed through the legislature so that politicians and other interested pressure groups can engage in lobbying and other

related activities to influence the legislative outcome. Truman's (1951) supposition that interest groups may attempt to place people who are sympathetic to their interests in key positions in the regulatory agency may be true in some, but not all situations.

In many of the political systems to which these theories apply, the regulatory agency is usually an independent agency or system. Eckert distinguishes between the degrees of independence associated with the independent commission and the regulatory agency. Since the cost-reward structures the regulator is faced with in both systems differ, it is expected that under identical scenarios the decisions taken in both systems may differ. However, in a political environment that is autocratic and dictatorial, such as under military rule, it could be difficult to assess the extent to which various interest groups are able to influence the peculiar decision making processes in such an environment. In such situations, the regulatory agency is not an independent body and the decisions it makes are usually, if not always, subject to approval by what Meier would call the "political elites." The political elites in this case could be described as the key members of the ruling military junta and their "power groups", who may be defined as those so close to them as to be able to influence their decisions relating to specific public policy. Thus under such conditions, although the head of a regulatory agency is appointed, the degree or extent of his regulatory powers vis-a-vis the rule making process may not be as extensive as it appears to be. Since he is not operating independently, he will have to take directions from the political elites and this could significantly influence regulatory decisions. It is conceivable in such situations that the head of the agency might be coerced into implementing rules with which he is not in agreement. In such a situation, it may not be in the best interests of industry groups to attempt to influence the key employees in the regulatory agency. If key regulatory officials have very limited executive powers, then it would not make economic sense for interest groups to attempt to place someone of their choice in key positions.

The implication for the various interest groups in the industry would be that they would have to determine, within their resource constraints, which one or which combination of the following groups; the head of the agency, members of regulatory committees, members of the ruling junta or other power groups, that it would be in their best interest to lobby. This could impose significant information costs (in terms of determining the groups that are most influential in the regulatory process) on interest groups. If the costs are excessive, the interest groups might decide that the effort was not worth the potential "benefits," which might not in any case (given the unpredictability of such a regulatory environment) be guaranteed to be in their interest.

In addition to this, even if the assumption is made, following Eckert (1973) and Noll (1971), that the regulator is a utility maximising individual, the maximisation of his welfare may not necessarily involve the pacification of the regulated industry by advocating regulation which will benefit them, as Eckert (1973) states. Instead the regulator may decide to play off both sides, the regulator and the regulated, along the lines of the cost-reward structure posited by Eckert, open to him. The degree of success he achieves in so doing will be determined by his political ability because this involves his ability to satisfy his "bosses", who have appointed him and who are subject to dismissing him on whim or caprice if he does not come up with the goods,[24] and his ability to satisfy the regulated industry. In such situations, the "minimum squawk" behaviour described by Hilton (1972), although it could involve the pacification of the industry (with for example promises to review and amend regulatory provisions not agreeable to the industry) does not necessarily lead to regulatory capture.

Meier's model, not surprisingly (since it has it's basis in the various theories) appears to be the most comprehensive of the regulatory theories. It recognises the fact that there are various interests represented in the regulatory environment and that their objectives and degree of influence or power they possess depends on the nature of the environment in which they operate. As such it can be employed in explaining, and perhaps predicting, the nature of regulation with regard to the various actors involved in the regulatory process. Since it is not premised on the assumption of a democratic environment and an independent regulatory agency, it can be employed in the analysis of regulation in almost any kind of regulatory environment.

2.3 Insurance Regulation

2.3.1 Insurance and The Public Interest

In his paper "The Purpose of Insurance Regulation: A Preliminary Enquiry into The Theory of Insurance Law," Kimball (1961) concluded that it was a difficult, if not impossible task to formulate a general theory of insurance regulation. His argument was that although common objectives of the regulatory process could be isolated, the "multiplicity of possible paths" to the accomplishment of these objectives "would seem to defy a definitive statement." He examined the pattern of evolution of

24. That is, keeping the regulated industry quiet at minimum cost to the government.

insurance regulation in the U.S and some European countries and observed that patterns of regulation had developed in specific response to "particular felt needs" in the system at the time, rather than as planned or anticipated policy action. In the U.S for example, a wave of regulatory reform followed after the scandal resulting from the New York Armstrong Committee hearings (Kimball 1961,p.477). Eight years later, Kimball (1969) considered his fears to have been justified. He commented on the lack of theory in the subject of insurance regulation. According to him, there was "no sense of a framework, of a carefully thought out basis for deciding what it is we want to do, no reflection upon the question where we are going, and why, no getting to the bottom of the subject."

A survey of the available literature does appear to indicate that the field of insurance (unlike the fields of, for example, transportation, electric utilities, and even banking among others) has been neglected in the economic analysis of regulation.[25] There have been various economic investigations into the industry, but these have been mostly into the analysis of the existence of economies of scale[26] and concentration[27] in the life insurance industry. Recently, probably as a result of discussions on the deregulation of markets, however there seems to have been a generation of interest in the field of insurance regulation.[28] The public interest aspect of financial markets has been specifically applied to the business of insurance and used as the main reason for the existence of the various forms of insurance regulation. The reasons are based on the "special" underlying characteristics of the insurance business which are supposed to distinguish it from most other forms of economic activity. This special nature of the insurance transaction can be found in the insurance literature that has been developing over the years. Bryan (1969,p.19)[29] distinguished the concept of security as being of primary importance in the regulation of insurance activity, stating that "in every subject there is a fundamental proposition...in insurance...that is that security is the one thing that is above all others." Wolfe (1972,p.165) as far back as 1906, spoke

25. Early (1974) discusses the lack of relevant literature in the area of economics and political science at length at pp.4-8. See also Joskow (1973) at pp.375-376 and more recently, Meier (1988) at for example, pp. xv, 1 & 167.

26. See, for example, in the area of non-life insurance, Hensley (1958), and life insurance, Johnston and Murphy (1957), at pp 140-146, Houston and Simon (1970), Pritchett (1973), Colenutt (1977), Geehan 1977 & 1985, Kellner and Matthewson (1983).

27. See Cummins et Al (1972), Colenutt 1975, Franklin and Woodhead (1980).

28. For example Ippolito (1973), Joskow (1973), and more recently Finsinger (1985) & (1986), and Meier (1988).

29. Bryan made these comments in 1914 at the National Convention of Insurance Commissioners in his capacity as Secretary of State of the United states. See Kimball and Denenberg 1969,p.17.

of the accumulations of a life insurance fund as a "sacred trust fund" and considered this to have been "one of the motives which lies at the very base of...supervision."

The special characteristics of the insurance service were identified as the future performance of the insurance transaction, its complexity, the unknown costs involved and the fact that it is a business subject to abuses (Greene 1977,p.552).[30] The fact that insurance activities were characterized by the inversion of the exploitation cycle has also been delineated as a special feature of the business (Van den Berghe 1990,p.213). However the view has been held that many of these reasons (specifically, the large amounts of money involved, the duration of the contract, its complexity, and what has been referred to as the "quasi-trust" idea) did not justify the comprehensive control of the insurance markets in existence in the United States (Kimball 1969,pp.4-5). For example large amounts of money are involved in the oil industry which is not as extensively regulated as the insurance industry, and most insurance contracts except life contracts are of short duration. He went on to say that there are other transactions that could be considered as complex as the insurance transaction (for example the purchase of a house) and the insurance contract was not technically speaking, a "trust", but merely a debtor-creditor relationship. Others, to varying extents, agree with this.[31]

Thus it appears that although researchers are basically agreed on the necessity for the existence of some form of insurance regulation, they are in disagreement as to the extent of regulation or the degree of control that is essential for the "efficiency" of insurance markets, in view of the fact that the regulatory system has costs associated with its operations. Identifying the costs is not an easy task, particularly as there are cost measurement problems (the lack of precise information on cost structures) as well as regulatory agency staff behavioural problems which are associated with their "intellectual and moral competence" (Kimball, 1969(c),p.1023). The controversy in British financial circles over the Financial Services Act (1986)[32] is illustrative of the problems involved in this area. It has led to questions being raised as to the effectiveness of "...the present cumbersome legalistic and costly approach..." in providing investors with adequate protection (Veljanovski 1988,p.10). Indeed the whole process of regulation has been criticised as at times being inefficient and ineffectual (Koch 1976,p.354). The most basic question to be asked and answered,

30. See also Bickelhaupt (1979), p.197-198.

31. For example Van den Berghe (1990) at p.207.

32. See Seldon (1988) for both sides of the argument.

before a consideration of the effects of regulation on insurance markets specifically, is "Why are we regulating?" or "What is the ultimate purpose or objective of regulation?"

2.3.2 The Purpose of Insurance Regulation

Various writers have somewhat similar views of the purpose of insurance regulation. Kimball (1969,pp.5-9) suggested that objectives of regulation could be classified along the following lines:

(1) The *Internal* objectives which he defined as those objectives that are directly related to the internal operations of the insurance business. These are;

(a) maintaining the solidity of the enterprise, that is the "preservation and enhancement of the solvency" of the enterprise and,

(b) ensuring fairness, equity and reasonableness [aequm et bonum] in the insurance market.

Kimball (1961) examined the evolution of the principle he called aequum et bonum[33] in the Swedish regulatory system. He referred to it as a "congeries of objectives" which were too vague to be expressed precisely, but were present to some degree in most regulatory systems. Fairness is concerned with the treatment of the individual policyholder by the insurance company. For example, claims should be handled fairly and agents should not make misrepresentations to individual policyholders or induce them to replace existing contracts with new ones on the basis of false or incomplete information (Kimball 1961,p.491). Equity refers to equity among the general body of policyholders and the principle involved is that insurers should treat their policyholders in a manner that is non-discriminatory. Simply put, policyholders should not be penalised unfairly by the terms and coverage of their contracts. For example, policyholders should be classified for fair calculation of the premium so that each policyholder pays only for the cost of his own protection (Kimball 1961,p.495). Likewise a life insurance company must distribute dividends equitably among its participating policyholders (Mayerson 1965,p.55). Reasonableness requires that the general body of policyholders be treated reasonably. Policyholders should not be

33. This concept comes from the Swedish term skalighet which had to do with reasonableness of the price paid for insurance and equity among policyholders (Kimball 1961).

overcharged and the terms of insurance coverage should not be ambiguous (Kimball 1961,p.491).

The requirements of fairness, equity and reasonableness sometimes conflict with and sometimes complement the requirement for solidity.

(2) The *External* objectives which though not relevant to the successful operation of insurance business are important because of their public policy content. They may be;

(a) political and/or

(b) socio-economic

Kimball (1961,pp.501-523) discussed the above in considerable detail. He described the political objectives of insurance regulation as democracy (egalitarian ideas in the social and political sphere) and liberty (that is the restraints on government interference with the insurance enterprise). Protectionism is the protection of the local insurance industry by placing localisation restrictions on its activities. Foreign insurers may be subject to restrictions on their activities which put them at a disadvantage in relation to domestic companies. This could be implemented on a local or international basis. The capital and licensing requirements may be more stringent and investment restrictions may prevent foreign insurers from investing in assets in their state or country of origin as the case may be.

Within the social and economic objectives are the needs for (i) the socialization of risk, that is, the provision of insurance coverage compulsorily (as in compulsory motor insurance) or the extension of existing coverage (as in assigned risk plans) on social rather than economic grounds (Kimball 1969,p.7); (ii) freedom of access to the market and (iii) the socio-economic aspect of investment control.

Other defined purposes of regulatory activity could conveniently fit into the above classification. For example, Mehr and Cammack (1976,p.650) have stated the underlying objective of insurance regulation to be the protection of the public from incompetent and fraudulent insurers, that is, aequm et bonum and apart from policyholder protection they also identify other objectives such as the assurance of fair competition, and the control of solvency supervision (solidity). Mayerson (1965)

reclassified Kimball's definition. He described the purpose of insurance regulation as being two-fold, solvency and equity, with equity encompassing the principles of reasonableness, impartiality and fairness. Franklin and Woodhead (1980,p.344), also referred to solidity as being the object of insurance regulation and supervision. Stewart (1969(a),p.24) proposed that the public purpose of insurance regulation was "...trying to help people get the most insurance for their money" (aequm et bonum), and argued that government has the social responsibility to see to it that the regulated industry responds to the current needs of society (Stewart 1969(b),p.35).

The various regulatory objectives detailed above are often in irreconcilable conflict. For example the requirement for freedom of access to the market conflicts with the requirement for the solidity of the enterprise. The regulator is faced with the problem of determining the level of capital and other licensing requirements that should be applied to the market. Too high a level raises entry barriers and facilitates concentration in the industry, while the solidity of the enterprise is called into question if the requirements are not adequate. Thus the regulator is faced with the problem of balancing the needs for the various objectives (Kimball 1969, pp.9-10)).

Comparatively speaking, little work appears to have been done in the specific area of insurance regulation. However the results of the available studies appear to lend support for the various political and economic views of the regulatory process discussed earlier on.[34] One of the conclusions of Joskow's (1973) study of the property liability insurance industry in the U.S was that the employment of prior approval regulatory laws were not necessarily in the consumers best interests. On the other hand, Ippolito (1976) in his study of the effects of price regulation in the automobile insurance industry in the U.S specifically tested to see whether the results of his analysis of price levels and price dispersion among other factors would support the Stiglerian hypothesis. His conclusion was that the results generally contradicted the theory (pp.63-67), and that the regulator attempted to maximise his welfare by satisfying the demands of various groups (including consumer groups).

Researchers in the field of financial regulation have nevertheless drawn attention to the fact that public interest theory is inadequate to explain the high levels of government interference in insurance.

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34. See sections 2.21 and 2.22.

For example, Van den Berghe (1990,p.207) examined the relevance of the public interest theory for all types of [European] regulation and government interference in insurance in the Belgian market in order to analyse the justification of the high level of government intervention in the industry. He stated that research had shown that although the application of the public interest character of the stability of the financial system to the area of insurance could provide an explanation for the high levels of government intervention in insurance markets, it did not justify all of the observed regulatory and supervisory measures in these markets. He posited that if, however, the special characteristics[35] of the financial sector were taken into account a separate "financial" public interest theory could be developed and applied to the field of insurance.

2.3.3 The Multi-interest theory of Insurance Regulation

Meier (1988) applied his multi-interest theory of regulation to the regulation of insurance in the U.S. He hypothesized that the various interests represented in the regulatory process would have policy goals which would be translated into policy measures. The resulting policy measures implemented in the industry would be dependent upon the resources of the actors in terms of their political influence. Since the actors would be in favour of goals that would be beneficial to them, industry groups would support regulation that benefited the industry and oppose regulation that placed burdens on it. In the same vein, consumer groups would be in favour of lower prices and restrictive regulation, regulatory bureaucrats in favour of restrictive regulation and increased regulatory authority while political elites would support regulation that was consistent with their policy values (p.137). In this scenario, the resultant policy measures implemented in the industry would be dependent upon the resources of the actors in terms of their political influence.

2.3.4 The Purpose of Insurance Regulation in Developing Countries

The socio-economic aspect of insurance regulation has been of increasing importance over the years, especially with respect to its supervision in the developing countries. The prevailing sentiment is that regulation should work to ensure that insurance company activities are coordinated with the socio-economic aspirations of a nation.

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35. (1) the fact that stability of financial markets is of crucial importance to the equilibrium of the economy, and (2) the confidential and fiduciary nature of financial products. (See van den Berghe 1990, pp.207-208).

In 1972, UNCTAD[36] published a report[37] which provided an analysis of the [then] existing legislation and supervision of insurance activities in developing countries.[38] The report among, other issues, examined the aims and objectives of insurance supervision in developing countries. The group of experts who produced it agreed that:

(1) the supervision of insurance was a "fundamental requirement for the sound development of insurance activities,"

(2) insurance activities when subjected to proper supervision played significant role in the economic growth of every country, and

(3) legislation should be developed in such a way as to furnish the basis by which insurance companies can be continually supervised, so as to ensure compliance with all aspects of legislation.

The report further stated that "insurance supervision, while playing the traditional role for which it had been originally established, namely the protection of policyholders beneficiaries and third parties, should also constantly take into account the general economic, social and other national interests," such as:

(a) the co-ordination of the investment activities of insurance companies with national economic policies and

(b) the prevention of foreign exchange outflows from excessive foreign insurance and reinsurance arrangements;

The committee of experts also specified what they regarded as a very important task of the supervisory process, "to provide for measures to establish and strengthen the national insurance market" since this is an "essential characteristic of economic growth". Thus it is the case that in most developing countries, while insurance regulation and supervision may have as the primary objective policyholder protection and protection against the risk of insolvency, in some others its purpose goes beyond this. The activities of insurance companies are often coordinated with national

36. United Nations Conference on Trade and Development.

37. Report TD/B/393, 1972, "Insurance Legislation and Supervision in Developing Countries."

economic activities. This is the case with Brazil and more relevantly Nigeria where government has attempted to co-ordinate the investment activities of the insurance companies with national development policies. Sometimes the insurance market is created and reconstructed with the purpose of promoting its growth and adapting it to national requirements. It has been observed that these objectives are usually not expressly stated in the relevant legislations and can be discerned only by interpretation.[39] Thus, while public policy towards insurance may be initiated to influence the balance of payments position and regulate the insurance companies flow of funds, much of it derives from the desire to govern the structure and behaviour of insurance markets in order to influence market performance (Shelp, R (1986,p.xx).

It can be seen that the professed purposes of insurance regulation are numerous, ranging from policyholder protection to nation building. There are, however, differences of opinion as to what are the "ends" and the "means" of regulation. Kimball (1969,p.16) argued that "...Very little consideration is given to the relationship of ends and means...we have often mistaken means for ends and have often been led into in pursuit of the wrong things." Achampong (1983) considered ideas for minimising this misdirection of the regulatory effort by suggesting that the focus of regulation should be on what he referred to as the "ultimate objectives" of regulation. He defined these purposes as the "end results" of the regulatory process, as opposed to the "means" by which these results could be achieved, the reasoning behind this being simply that "they [the end results] cannot be subsumed under a further or more fundamental objective" (see p.301). He went on to apply the "ultimate objectives" test to some of the regulatory objectives in order to identify their means and ends. For example, in considering the condition of solidity, he stated that it could be seen as a means of achieving the ultimate objective of policyholder and beneficiary security, with rate regulation and control of investments being ancilliary means to this objective.

2.4 The Scope of Insurance Regulation

The scope of regulatory possibilities in the context of public policy concerns is quite wide and extends somewhat beyond the common perception of public control of

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38. The objectives, nature and scope of insurance legislation in developing countries is examined in some detail in chapter 3.

39. UNCTAD TD/B/393,pp.28-29.

private social and market related activities (Mitnick 1980,p.14). Mitnick (p.5) as stated earlier defined a "typology of regulation" in which he isolated four possibilities of regulation among public and private parties: (1) traditional regulation (public regulation of private activity); (2) capture (reverse regulation); (3) private self-regulation; and (4) government regulation.

Insurance regulation was stated to fall within the first three areas and the broad scope of regulatory activity[40] is concerned with the activities of insurance companies with respect to the ensurance of compliance with laws affecting the legal, technical and financial requirements of the business of insurance (Bickelhaupt 1979) as well as the socio-economic aspects of the business in relation to the development of the economy.[41] For the purpose of this discussion, the scope and nature of insurance regulation may be defined along the following lines:

(1) Financial regulation

(2) Product regulation, and

(3) Business methods regulation of insurance business (Mehr and Cammack 1976,p.680).

The constraints on the effective discharge (by a regulatory agency) of regulatory functions associated with the above are a function of (a) the financial resources of the agency, (b) the quality of it's personnel, and (c) the philosophy of the head of the agency (Mehr and Cammack, 1976,p.680).

2.4.1 Financial Regulation

Financial regulation is concerned primarily with ensuring insurer solvency. It involves the regulation of areas such as premium rates, expenses of operation, valuation of assets, technical reserves, capital stock and surplus, dividends, investments, legal requirements as to the organization and licensing of insurers, and the liquidation of insurers (Mehr and Cammack 1976,p.680).[42] An analysis of some of these areas could be an indicator of the efficiency or otherwise of insurer operations under differing

40. Hellner (1963) discusses the scope of insurance regulation in detail.

41. UNCTAD op.cit. p.29.

regulatory regimes and as such some of the regulatory requirements in these areas are examined briefly below.

(1) Premium Rates

The purpose for the regulation of premium rates is to ensure that the rates are, among other things, not excessive so as not to penalise policyholders unfairly, and at the same time not inadequate so that the solvency of the insurer is maintained at all times. Thus premium rate regulation should satisfy the objectives of equity, reasonableness and solvency. These requirements are codified in the All-Industry laws passed by the states in the U.S that insurance "rates shall not be excessive, inadequate, [or] unfairly discriminatory" (Kimball 1961,p.482). The requirement for equity is difficult to attain. For example, motor insurers commonly place an excess on young and/or inexperienced drivers because of the high probability of loss which has been estimated from past experience. However, that is not to say that every young or inexperienced driver will be involved in an accident. In such situations therefore, a group of policyholders is being discriminated against.[43]

The provisions for the regulation of insurance rates vary. In most cases, prior approval laws are utilised. This means that the insurance concerns have to submit to the supervisory committee the rates they propose to charge on the various classes of insurance business for approval. The rates are usually filed with the appropriate statistical justification of the level of the proposed rates. The same process is usually needed before an increase in premium rates can be implemented by the insurance companies.

Although the purpose of rate regulation is to ensure the fairness, non-excessiveness and adequacy of rates, studies in this field indicate that the attainment of these objectives may in fact be hindered by the process of regulation.

Frech and Samprone (1980) attempted to measure the welfare loss associated with rate regulation in property-liability insurance in the U.S between 1972 and 1974. They concluded that the costs of price regulation in this sector of the industry outweighed the benefits, especially for liability insurance. Witt and Miller (1980) also arrived at the same conclusion. They compared the relative costs for automobile

42. See also UNCTAD TD/B/393, pp.27-29.

insurance under competitive and non-competitive[44] regulatory regimes for the years 1971-1978, and argued that since there were basically no differences in relative costs in both regimes, then by implication, consumers in the competitive states were better off than those in the non-competitive state. They concluded that it seemed there was no "empirical economic justification" for automobile rate regulation (p.184). Further study (Witt and Miller 1981) led them to suggest that rate regulation rather than preventing insolvency, tended to increase the probability of insurer insolvency in this sector, and may actually impair market efficiency (Joskow 1973; Ippolito 1979;, and Nadel 1982).[45]

(2) Expenses

Expenses are regulated as an indirect means of controlling premium rates. In life insurance, expenses, future interest rates and mortality experience are factored into the premium charged for coverage. The regulation of this item usually involves the regulation of acquisition costs, that is the cost of obtaining new business, including agents and brokers commissions. In some cases limits are set on first year and total field expenses, as well as renewal commissions (Mehr and Cammack 1979,p.683).

(3) Asset Valuation

Asset valuation is a very important aspect of solvency measurement. For an insurer to be solvent the value of his "admitted assets" must at least be equal to the value of his liabilities. Regulations may therefore specify the nature of the assets which the insurer may take into account in determining the solvency of the insurer. Such assets are referred to as admitted assets. Additionally the method by which such assets may be valued may be regulated. For example, the valuation of cash and bank deposits may be on the face amount of these assets while real estate may be valued at book or market value (Mehr and Cammack 1976,p.684).

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43. Kimball (1961,pp.495-499) discussed the issue of equity at length.

44. Witt and Miller defined competitive regimes as operating in states where competitive market forces were allowed to determine premium rates in the market, and non-competitive regimes as operating where the states in one form or the other regulated or constrained rates by not allowing market forces to operate in the setting of rates.

45. See Harrington (1984) for a survey of research in this area.

(4) Reserves

Different types of reserves are required for the various kinds of insurance business underwritten. The purpose of holding reserves is to cover the liabilities of the insurer to policyholders, beneficiaries and third parties under the insurance contract. These liabilities are in the form of claims payments. Some of these reserves are; the unexpired risk reserve, the reserve for outstanding claims and the mathematical reserves.

To ensure insurance solvency, the role of the supervisory authority is to see to it that the actuarial valuation of these reserves is such that at all times the insurers liabilities to the aforementioned are covered. The degree of latitude allowed to insurance companies in calculating their reserves varies from country to country. In some countries, the regulations are liberal and the insurance companies are allowed considerable degree of freedom in the method and basis of the valuation of the reserves. At the other end of the scale, there are places in which the supervisory authority does not ensure a minimum level of solvency because there are no relevant provisions for doing so in the regulatory law. In fact, in many developing countries where minimum level of solvency regulations are in force, it is found that the regulation of technical reserves is more often a theoretical rather than practical affair and that the effectiveness or otherwise of the law is entirely dependent on the technical competence of the supervisory authority. In the developing countries reserves play a dual role, that of maintaining insurer solvency and as a potential source of development capital.[46] The following reserves are maintained for non-life insurance business:

(i) The Unexpired Risk Reserve

The unexpired risk reserve is defined as the "unearned portion of the gross premiums of all outstanding policies at the time of valuation" (Mehr and Cammack, 1976,p.627). Non-life insurance contracts are annual contracts, with premiums being payable at any point during the financial year. Consequently when the insurer draws up his balance sheet at the end of the year, there will be some risks on the books for which he has received premiums, but for which he is still liable for the duration of the policy year.

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46. See UNCTAD, op.cit pp.49-50.

For example, if as at the balance sheet date, the insurer has received an annual premium for a risk which still has nine months to run, then he is still liable for the unexpired or unearned portion of the risk for which he has received the premium. This is covered by the "unexpired risk" or "unearned premium" reserve. In some of the developing countries[47] studied by the UNCTAD experts the figure for this reserve was arrived at by applying a fixed percentage to the premiums due during the year. The percentage used varied from 30 to 50%, 40% being the most preferred figure.[48] It was noted however, that at that time, the English-speaking African countries, among others, did not impose any regulatory requirements in this area.

(ii) Reserves For Outstanding Claims

This reserve "measures the insurer's estimated liability for claims and settlement expenses as of the valuation date" (Mehr and Cammack 1976,p.629). In other words it covers the insurer's liability for claims accepted by the insurer but for which the compensation remains unpaid at the date of valuation. It includes:

(a) reported and adjusted claims which have not been paid,

(b) claims which have been filed but not yet adjusted, in that the amount of compensation to be paid by the insurer to the policyholder has not been agreed to by both parties,

(c) claims incurred but not yet reported (Mehr and Cammack 1976,p.629), and

(d) claims in connection with current life or annuity business which are aleatory and are calculated actuarially.[49]

The method of estimation of outstanding claims varies across countries. The amount estimated may depend on the subjective influence of the company making the valuation and the only way in which to ascertain whether the valuation has been made correctly is by means of an a posteriori verification, that is by comparing the actual figure with estimated the amount. Some developing countries, for example, Cameroon, Brazil, Trinidad and Tobago have however tried to rectify the situation by

47. For example, Morocco, Egypt, Lebanon, Ceylon, Israel, Malaysia, Pakistan, among others.

48. UNCTAD op.cit.p.51.

having specific regulatory requirements that make for a more objective method of calculating this reserve.[50]

(iii) Contingency Reserves

The contingency reserve is set up as a "compulsory supplement" which serve to make up for any inadequacies in the other technical reserves. As with the other reserves, its provisions may vary across countries.

(iv) Mathematical Reserves

This is the major reserve held for life insurance business. Broadly speaking, it is "the amount, needed to cover all policy obligations as they become due (Mehr and Cammack, 1976,p.631). The method of calculation of the reserves or the technical basis upon which such calculations are based may be specified by law.[51] In practice, the valuation of reserves is a difficult task, not only for the insurance companies, but more so for the supervisory authorities.

(5) Investments

Regulatory rules covering the investment of the funds of insurance companies are concerned with the qualitative and quantitative restrictions on the investment choice of the insurer (Mehr and Cammack 1976,p.689). The qualitative rules prescribe the different types of assets into which the insurer is permitted to channel his funds, while the quantitative rules establish minimum percentages or maximum ceilings allowed for the various types of investment media. Regulations usually require the insurer to invest a minimum percentage of his assets in government stocks and bonds, while restrictions are placed on the amount of speculative securities, such as equity stock, that the insurance companies may invest in order to maintain solvency. For the non-life fund, the investment portfolio has to maintain some degree of liquidity since the insurers liabilities are of a short-term nature. The life fund on the other hand, may be invested in longer term less liquid assets since life contracts are usually of a longer

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49. UNCTAD ibid.p.52.

50. UNCTAD ibid.p.53.

51. UNCTAD ibid.p.50.

duration. The rules usually prohibit the insurer from obtaining a controlling interest in non-insurance business.

The regulations in developing countries, are usually more restrictive than those applied to the advanced economies. This is pursuant to the objectives of the supervisory authority, that is, ensuring the solvency of the insurer and covering the investment needs of the economy.[52] For example, there is usually a restriction, in most cases a prohibition, on the insurer holding foreign assets in his investment portfolio. The purpose of this "localisation" of insurance funds is to ensure that scarce capital is retained in the country for development purposes.

(6) Organisation and licensing requirements

These requirements seek to prevent incompetent and/or fraudulent persons from establishing insurance companies. The legal form of insurance companies is specified by law. Insurance companies in most cases are allowed to take the form of limited liability companies and mutuals. Additionally, prior authorisation to engage in the business of insurance may be required.[53] This authorisation may be granted under or pursuant to an administrative act or decree as the case may be, the supervisory authority acting as an advisory body to the minister responsible for the authorisations. In some cases, the granting of authorisation is left to the supervisory authorities. The insurer may only engage in activities that are directly connected with insurance business and no individuals or partnerships may set themselves up as insurers.[54] In some cases, applicants for licensing for life insurance business are required to submit to the appropriate authority a business plan which gives a projection of the insurers business during the first few years of operation and stipulates how the insurer expects to meet his future obligations under the contracts he propose to underwrite.

In the U.K, The Insurance Companies Act 1974 stipulates that the business plan should include the following information: pessimistic and optimistic estimates of the expected volume of business over the first three years of the company's operation, estimated expected number of policies, types of policy and sums insured in respect

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52. UNCTAD ibid.p.60.

53. UNCTAD ibid.p.35.

54. UNCTAD ibid.p.9.

thereof. In addition, information such as revenue accounts showing the expected income and expenditure, commissions and size of funds as well as proposed premium rates have to be given (Franklin and Woodhead 1980,pp.93-94).

These requirements in most cases apply to both domestic and foreign insurers operating in the industry. In developing countries protectionist legislation is employed to protect the local industry from foreign domination and capital flight to the more advanced economies. If an insurer is to be regarded as domestic, then foreign participation in the insurance company is limited either by specific provisions relating to the insurance industry, or by laws which apply to the economy as a whole. In some cases the regulatory requirements in respect of foreign insurers are more stringent than that of domestic insurers. The regulations make provision for the classification of insurance business generally into life and non-life business, and specify the requirements for the application for registration, as well as the grounds for the cancellation of registration and liquidation of the insurer. For example, registration may be cancelled where insurance business is not being conducted in accordance with sound insurance principles, or where technical reserves are inadequate, among other things.

The required share capital for each class of insurance (and reinsurance) business is also set out in the law. Sometimes the amount of share capital required in the case of foreign insurers is much higher than that of the domestic insurers. Regulatory provision may be made for the treatment of share capital. The supervisory authorities require insurers to maintain and submit in accordance with regulations, specified financial reports for example registers of assets, claims and policies. Annual reports and accounts in respect of insurance business also have to be submitted as laid down by the rules. There are usually additional requirements with respect to life insurance business such as the actuarial valuation report, summary and valuation of life policies, tables of premiums policy reserve values and guarantee surrender values, with the relationship between premiums paid and such surrender value.

2.4.2 Product Regulation

Insurance is an intangible product. Since it is basically a service activity, product regulation essentially involves insurance policy form appraisal and approval, since the policy is the written evidence of the contract between the insured and the insurer. The policy forms, general contract terms and conditions as well as insurance certificates

are submitted to the supervisory authority before the commencement of insurance business and approval of these documents by the supervisory authority is an essential prerequisite to the commencement of business.

The purpose of doing this is to protect the interests of the policyholders under the contract and to ensure that the contracts have a legal basis. The aim is to prevent policies with contract terms that are ambiguous, deceptive or detrimental to policyholders from being issued. Insurance contracts are also examined to ensure that they do not conflict with the relevant insurance laws or commercial law (Mehr and Cammack 1976, p.694; UNCTAD TD/B/393,p.9). Policy form approval satisfies both the principles of reasonableness and fairness (Mayerson 1965,p.54).

2.4.3 Business Methods Regulation

Business methods essentially involves the marketing practices of insurance intermediaries and its regulation is aimed at protecting the insuring public from incompetent and dishonest insurance intermediaries and to maintain fair competition in the market (Mehr and Cammack 1976,p.700). This is put into practice by (1) the specification of licensing requirements of agents and brokers and (2) the prohibition of some practices such as misrepresentation, twisting and rebating. In some cases advertising material and sales literature are examined to ensure that they do not contain any information that is deceptive or misleading (Mayerson 1965,p.56).

The requirements in respect of brokers are more stringent than that of the agents because of the greater responsibility placed on brokers who are deemed to be professionals with a higher degree of expertise. The requirements are both financial (licensing fees) and organisational. The organisational aspect involves the establishment of minimum qualifications for prospective agents and brokers, the duties of both categories of intermediary as well as requirements as to the their general conduct. Generally licences are issued for a year and in some cases, agents may be required to take and pass a written examination administered by the relevant insurance association or other accredited examining body before a licence is issued.

Regulatory requirements may prohibit "twisting" that is the inducement of a policyholder by an agent to substitute one insurance contract for another (Mehr and Cammack 1976,p.696). Agents do this in order to earn commission on new contracts since renewal commissions are usually much lower than first year commissions on

new contracts. "Rebating" laws are designed to maintain fair competition among agents. This occurs where agents in their efforts to secure a contract with insureds refund part of their commission to them (Mehr and Cammack 1976,p.696). The classification of rebating as an uncompetitive activity has been challenged (Yakubu and Mukubwa 1986,pp.15-16). These regulatory provisions ensure that the policyholder is treated fairly.

The scope of insurance regulation varies from country to country and also across lines of insurance business. Insurance business may be subject to a close system of insurance supervision whereby practically every aspect of the insurers activities are regulated. On the other hand the business may be subject to fiduciary control, in which case supervision relates to only those aspects that affect insurer solvency.

Summary

The regulation of economic activity has been justified by the necessity to ensure that the public interest is protected. Economic theory defends this on the premise that market imperfections are inimical to consumer welfare. However, some theorists have postulated that in many cases, in the public regulation of private activity, producer interests, and not the consumer interest are served because powerful pressure groups within the regulated industry have "captured" the regulatory agency.

The extensive regulation of the insurance industry has been justified on the basis of the fact that the insurance contract is fiduciary in nature and the existence of information asymmetry between the sellers and buyers of insurance services. In developing countries, the regulation of the insurance market is seen as being essential in co-ordinating the activities of insurers with national development policies. The scope of insurance regulation varies across markets, and while extensive regulation of insurance markets may be undertaken, it has to be recognised that the regulatory effects of such intervention may not necessarily be in the public interest. This issue is particularly important with respect to developing country insurance markets which are still in the early stages of development. It is thus vital to ensure that regulatory policy employed in such markets are selected within the context of the socio-political environment, in such a way that growth of the market is encouraged and not inhibited.

In the next chapter, the costs and benefits associated with the employment of various regulatory measures in developing country markets are examined within the context of the political economy of these markets. This will form the basis for the analysis of regulatory policy in the Nigerian life insurance industry.

Chapter 3

The Insurance Industry in Developing Countries

Introduction

Insurance in general and life insurance in particular have significant contributions to make to the sphere of economic and social activity. Life insurance is said to play an important role in financial intermediation.[1] The degree of the significance of this role has been found to vary with the level of a country's economic development, and generally speaking, insurance activities attain more importance in the more developed economies. The linkages between financial development and economic growth in underdeveloped countries is discussed in the economic literature[2] and developing country governments will attempt to influence the growth of financial markets, and by implication the economy, by employing various financial policies which are aimed at stimulating growth in the markets. Many of the policies utilised in the insurance markets in such economies are protectionist in nature. The necessity for, and efficacy of, these policies in stimulating insurance market growth in developing economies has generated some debate.[3]

It follows that in order to facilitate an understanding of the development of the regulatory philosophy in markets generally, a knowledge of the economic and political developments in the economy is essential. In this chapter, the characteristics of insurance markets in developing economies is examined, and the various arguments for and against the implementation of protectionist interventionist policies in these markets are discussed. This is intended to form a basis for the discussion of the development of, and regulation of the Nigerian life insurance market within the context of developments in the Nigerian socio-political situation.

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1. See chapter one.

2. For example Patrick 1965 and Engberg 1988.

3. Discussed further on in the chapter.

3.1 The Demand for Insurance

The demand for insurance[4] increases with the rate of economic growth and development and the importance of the insurance sector in the economy varies from country to country. This variation in demand can be attributed to first, the demand for the underwriting of risks, and secondly, the types of risks insured, as well as financial market structure, and government regulation (Hill 1986,p.121).

This demand has been found to be positively correlated to the level of personal disposable income in the economy so that countries with a high income monopolise the demand for insurance. Generally speaking the demand for insurance (and, by implication, the volume of premium income) grows faster than national income, so that the contribution of insurance to GNP is more significant in the developed countries than in the developing countries (Diacon 1980; Wasow 1986; Hill 1986). In support of this assertion, Wasow (1986,p.161) states that in 1982, the ten largest insurance markets in the world were developed country markets. These markets accounted for 90% of world-wide insurance premiums while in the less developed countries (developing countries), the ten largest insurance markets accounted for only 3% of world-wide premiums. His analysis of the relationship between per capita income and premium volume for 45 developed and less developed countries (1982 figures, including Nigeria) demonstrates that insurance penetration[5] increases with rising income, especially with respect to non-life insurance.

The differences in the relative significance of the insurance sector in the developed and developing economies can also be explained by other factors apart from per capita income. Wasow (1986,p.161-173) identified a number of structural and policy variables which influence the size of a country's insurance market. These structural variables are expected to influence the demand for insurance while the policy measures should have a more significant effect on the supply side, although this is not always the case as some policy measures could have some effect on demand. For example, protectionist policies towards the local insurance industry, nationalization[6] or licensing could affect both the demand for and supply of insurance services by increasing or reducing the confidence of consumers in the industry. These effects

4. See Diacon 1980.

5. Premium income relative to GNP, Wasow (1986) at p.161.

6. Discussed further on.

create uncertainties in the prediction of the effect of policy on the demand for insurance (Wasow 1986,pp.165-166).

The structural variables examined by Wasow in his study were (1) the levels of money supply relative to GNP, (2) government spending relative to GNP (3) the rate of inflation, (4) service imports relative to GNP, (5) the output capital ratio, (6) gross savings relative to GNP, and (7) the Islamic factor. The results of various regression analyses Wasow employed indicated that:

(1) a low penetration of life insurance was associated with high levels of saving and inflation, and

(2) nationalization, compulsory premium cessions to government institutions and restrictions on the remittance of profits appear to reduce life insurance premium volume.

(3) predominantly Islamic countries were characterised by a lower degree of insurance penetration.

It has been argued that the relationship between insurance premium income levels and national income is more significant and more stable for non-life than life insurance, and that financial market structure, and government policy, as well as the rate of inflation, have a stronger influence on the demand for life insurance (Hill 1986,p.122; Wasow 1986,p.162).

Insurance has many benefits and[7] life insurance in particular has a significant role to play in the development of a country.[8] Apart from the provision of protection for individuals in society, it can aid development by among other things, creating a source of financing for new business, generating employment, and encouraging the undertaking of the risks incidental to business activities (Shelp, J. 1986).[9]

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7. Insurance also has it's costs. These costs are in relation to the moral and morale hazards presented by policyholders which may increase loss costs to both the insurers and society at large. See Mehr and Cammack (1976,p.13), and Bickelhaupt (1979,pp.52-54).

8. Discussed earlier on in chapter one.

9. See also UNCTAD 1982, TD/B/C.3/177, "The Promotion of Life Insurance in Developing Countries."

Empirical studies have provided strong evidence of the close positive linkages between real growth of the economy and the real growth in financial assets, in both industrialised and developing economies,[10](Engberg 1986,p.2). Financial intermediation is essential for the channelling of real resources from the savers to the investors in the economy. Specifically in the case of life insurance, the conditions that encourage its growth in developing economies have been identified as follows:

(1) adequate infrastructural facilities such as communication, transportation, health care, legal and education systems,

(2) conditions that may create a demand sufficient to sustain the growth of the business, such as a fairly well developed manufacturing and service sector

(3) the presence of institutions and companies that can meet such demand and

(4) an economic and legal environment conducive to the growth of the business.[11]

The absence or inadequacy of one or more of these factors will inhibit the demand for life insurance.

Engberg affirmed that in most of the developing countries with which he had been associated, the financial structure of the capital market has been a hindrance to economic development because the policymakers have failed to recognize the importance of finance to economic development. As a result, their interventions in the financial sector have been unsystematic, haphazard and counterproductive (pp.111-114). These [interventions] had led to some distortions such as the imposition of unrealistic interest rate ceilings, overvaluation of the domestic currency, financing of government through the financial sector, the collusive acts of financial institutions to restrict competition, as well as their reluctance to expand financial services to new geographical areas (Engberg 1986,pp.115-117). The distortions had resulted in

> "a patchwork of specialised financial institutions, each pursuing it's own narrow objectives with little coordination of efforts;...and...financial policies consist of a hodgepodge [sic] of controls and regulations that are more likely than not to prevent the

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10. See Patrick 1965 for a treatment of financial development and economic growth in developing countries.

11. UNCTAD 1982, TD/B/C.3/177,pp.3-9. See also Nabolz (1986,pp.34-38).

> financial intermediation mechanism from playing it's proper role in the economic development process" (p.118).

3.2 The Insurance Industry in Developing Countries

Shelp (1986) attempted to interpret the role of services in economic development. He argued that development strategies have focused mainly on the development of the manufacturing sector. These strategies have not been centred on the development of the service sector, nor have they emphasized the importance of the service sector in the process of economic development. According to him the failure of economists in the industrialised nations to investigate the service sector has resulted in the development of inadequate and inconsistent theories of economic development. These theories have been transferred in their deficient form to the developing economies who, despite this inadequacy in theory, seem to recognize the important role of services in the economy. However their progress in the development of the services sector in these economies has been marginal (pp.3-5).

Nabolz (1986,pp.34-48), examined the relative importance of the insurance industry in developing countries and was of the opinion that these countries were accommodating many new markets with large growth potential. He attempted to isolate some "common determinants" which he felt were characteristic of the majority of insurance markets in developing economies. Nabolz's findings were that, generally speaking, insurance markets in developing countries had the following characteristics:

(1) They were former colonies, many of whom were still trying to find their political identity. The social structure in these countries had led to a politically unstable climate which affected the environment in which insurance companies had to operate.

(2) Economic conditions were difficult. Many of the countries were still largely dependent on "low productivity agriculture" and unemployment was high. To the extent that economic conditions affect the volume of insurance and reinsurance business as well as the ability of the insurance market to obtain necessary insurance protection from abroad, this is an important determinant of the size of the insurance market.

(3) Inefficient and inadequate communications and transportation systems, which served to hinder business activities.

(4) Pervasive government participation in the insurance industry. Although the availability of insurance protection is essential for successful economic development, in many developing countries this sector of the economy has been neglected by indigenous private investors. Consequently, the government has had to intervene in various ways in order to provide or increase the availability of insurance services in the economy.

(5) The insurance portfolio of companies in developing country markets is usually unbalanced being dominated by a preponderance of motor insurance business. This could be attributed to the compulsory motor vehicle third party insurance legislation in force in these countries, as well as the fact that the insurance markets are small.[12] The results of motor insurance business in most countries is unprofitable.

(6) Market development is hindered by the lack of indigenous management personnel, and

(7) Available underwriting material is ill-suited to local conditions.

Nabolz (1986,p.41) also demonstrated that where the insurance industry is developing freely, there is a positive correlation between the ratio of insurance premiums to GNP (as well as per capita premium) and the rate of economic development. In other words, there is a relationship between the rate of development of the insurance industry and the rate of economic development (Diacon 1980; Wasow 1986; Hill 1986). Thus if growth is stimulated in one sector, through public policy measures, this will affect the development in the other sector.

Another characteristic of developing country insurance markets is that the control legislations in some of the markets had, in the past, been patterned after the legislations of their colonial masters, irrespective of whether or not they fitted in with the socio-economic aspirations of such countries (Ripoll 1974,p.75; El-Hassan 1981,p.43; Nwokolo, 1986,pp.106-107).

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12. UNCTAD 1980, TD/B/C.3/163/Add.I, "Third World Insurance at the End of the 1970's."

3.3 Government Intervention in Developing Country Markets

The nature of government intervention in developing country markets has taken various forms;

(a) Nationalisation of the insurance market.[13] Such markets are monopolistic with the government holding the general monopoly of insurance business.[14]

(b) The establishment of government owned insurance companies that compete with private indigenous insurers. The government sponsored companies usually enjoy certain advantages over their private counterparts, such as tied[15] business.[16]

(c) The establishment of government insurance companies which operate as joint ventures with private local and/or foreign insurers.[17]

(d) The establishment of local government sponsored reinsurance institutions[18] as well as regional companies and reinsurance pools. The pools are meant to facilitate co-operation between countries in the region for the benefit of local and regional insurance markets. Government compels companies operating in the market to cede a specified proportion of their premium income to these national reinsurance institutions and pools.

The genesis of the establishment and implementation of nationalistic or protectionist policies in the developing country markets was facilitated by the co-operation of the UNCTAD secretariat. These countries had come to the realisation that a significant amount of funds in the form of direct insurance premiums and reinsurance premiums

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13. For example, Angola, Algeria, Afghanistan, Cuba, Libya, Ethiopia, India Guinea, Madagascar, Mozambique, Swaziland, Tanzania, Zaire, and Zambia (UNCTAD TD/B/C.3/169/Add.I)

14. See UNCTAD TD/B/C.3/169/Add.I, ibid. UNCTAD classifies categories (b)-(d) as pluralistic markets.

15. This occurs where the insurance of all government property may be handled only by the government owned insurance companies.

16. For example, Nigeria.

17. For example, Nigeria.

18. For example, Brazil, Trinidad and Tobago Ghana, Kenya, Nigeria, Sierra Leone, Kuwait, Morocco, Pakistan, Korea (UNCTAD, TD/B/C.3/169/Add.I), Brazil, Nigeria and Tanzania.

was being remitted to the developed country markets as a result of their activities in these markets. In colonial times, these funds were directly extracted from the developing countries through premium and profit remittances abroad by western

insurers. Although this practice had stopped with the independence of the developing countries and subsequent implementation of some form of protectionist measures, many of these countries were still largely dependent on western insurers, and the extraction of surplus still continued under the veil of reinsurance activities (Ripoll 1974, El-Hassan 1981).

In order to assess the situation, UNCTAD investigated the insurance and reinsurance activities of developing countries. Subsequent to the investigation, it conducted the first of many sessions in July 1964, during which a number of recommendations were tabled. The recommendations emphasised "the need for developing and strengthening the insurance and reinsurance markets in the developing countries" and agreed that in order to do this a number of measures would have to be implemented, viz

(1) Increasing retention capacity in the markets so as to reduce the outward flow of insurance and reinsurance funds to developed country markets;

(2) Promoting insurance business in order to increase the level of savings and investment in the economy and,

(3) The provision of reasonably priced insurance protection for industrial and economic activity.[19]

In order to achieve these objectives, the governments of many developing countries have actively intervened in insurance market operations with a view

> "To protect policyholders, limit foreign exchange liabilities, ensure the provision of insurance services, prevent an excessive proliferation of insurance companies, and generally to encourage a healthy environment of, and promote efficiency in, the insurance market."[20]

With regard to the establishment of national reinsurance concerns UNCTAD saw the main advantages of such institutions as including the reliable recording of insurance

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19. See Journal of World Trade Law, 1967,pp.229-230.

business operations, the increased total retention capacity of the national market, risk redistribution among local companies and the improvement of the bargaining power of the local companies vis a vis the international reinsurance markets.[21] Since then the case for nationalistic (that is protectionist) regulation in developing country markets has been extensively examined and has been said to depend on some combinations of the following basic arguments;

(1) Foreign insurers make excessively high profits in local insurance markets,

(2) The purchase of insurance and reinsurance services from abroad puts an undue strain on the developing countries balance of payments position,

(3) Insurance funds which could be channelled into development purposes are more likely to be invested abroad so that the growth of the local market is impaired,

(4) The dominance of foreign insurers in the insurance market prevents indigenous personnel from acquiring necessary expertise in insurance business,

(5) Developed countries such as Japan, Germany and France among others also protect their national insurance markets, and as such developing country markets would do well to pursue the same strategies (Hindley 1982,p.13).

The above issues have been the subject of considerable debate and many of the above arguments have been considered to be untenable. Wasow (1986,p.90) argues that there is no evidence that international insurers are making excess profits in developing country markets, while Hindley (1982,p.14) believes that if and where excess profits are being made this has been caused not by the activities of foreign insurers but by restrictive barriers to entry imposed in the markets by the developing country policy makers. Although the possibility of foreign insurers charging higher prices than local companies is acknowledged, the higher prices are said to reflect the higher quality of service they provide (Carter and Dickinson 1979,p.38). El-Hassan (1991,pp.34-35) argues to the contrary. He cited Britain as one country that has gained immensely from its operations in underdeveloped markets to the extent that the British policyholder was being subsidized by the consumers in developing country

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20. See Journal of World Trade Law, ibid. p.230.

21. UNCTAD 1972, TD/B/393, "Insurance Legislation and Supervision in Developing Countries," p.16.

markets[22] in consequence of which it is the "most vocal antagonist" of protectionist policies in these markets.

He suggested that Britain's support of the "freedom of insurance" doctrine[23] could be attributed to self interest since the country has made immense profits from its overseas insurance business. Ironically although the doctrine is advocated by the developed markets, the available evidence suggested that in practice, developed country insurance markets did not pursue this policy.[24] The activities of some EEC member countries in this regard is worth considering. A quote from The Economist of 12 February 1972 in Ripoll (1974,p.84) illustrates the point:

> "A British Insurance Company, applying to the French insurance control authorities in the usual way for permission to underwrite in Paris was kept waiting for so long that it finally demanded an explanation. In reply it was told that things would be easier if foreign companies could get into the Institute of London Underwriters, the club of the company marine underwriters in the London market...It then emerged that other British companies had also been getting nowhere in their applications to write in France. French insurers are not alone on the Continent in their complaint that in practice the London insurance market...is hard to get into, even though in theory it is open to all comers having routine Department of Trade and Industry permission".

Similarly, in recent years the US, as a result of the relatively small percentage of world service exports and the growing limited capacity of the domestic market, have been supporting the concept of the liberalisation of trade in insurance services. Protectionism is said to be "...a threat to international trade and to US national interests" and it is considered that liberalisation would secure the benefits of increased sales for the American insurance industry, since their expertise in the area of pricing and products amongst other things are often superior to those of the developing countries (Skipper 1987,p.64).[25]

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22. See also Ripoll (1974) at pp.77-80).

23. The principle that the restriction of the supply of insurance by foreign insurers results in the unavailability of suitable insurance cover at affordable prices.

24. Carter and Dickinson (1979,p.2) state that practically all countries practice in varying degrees some form of discrimination in this regard.

25. Skipper 1987 however concludes that though " the US insurance industry has a vested interest in minimizing protectionism...[t]his interest does not conflict with the concept of economic efficiency gains; it reinforces it."

In order to increase their volume of business many of these developed country insurers have to implement expansionist programmes which are naturally directed towards third world insurance markets which offer the least degree of resistance by reason of their comparative underdevelopment. In fact, western insurers have found it extremely difficult to penetrate into other western insurance markets (Ripoll 1974,pp.76-77,84-85). It appears that the developed country markets have not been averse to employing some form of "coercion" to implement their expansionist programmes. UNCTAD notes that "A major inducement for liberalisation has been provided by international lending institutions, generally under `conditionality' programmes...particularly in Africa..."

Such moves have met with vigorous opposition in the third world markets. In June 1988 the 15th General Assembly of the African Insurance Organisation appealed to all African Governments

> "...to recognise that insurance is a vital tool for economic emancipation and growth and as such its control and basic utilisation should be in the hands of the nationals who are totally committed to the development of the country's economy."[26]

Despite this however the developed countries are intent on pursuing the policy of liberalisation in services in general and insurance services in particular.[27] Because of the belief that the purchase of international insurance and reinsurance services strains the balance of payments position, governments have implemented, in line with various UNCTAD recommendations, various "defensive" policy measures to address this issue. Such policies are usually part of a general commercial policy which is applicable to several subsectors of the economy.

Not surprisingly, the western insurers were not supportive in this respect. They in fact accused the developing countries of being paranoid about the issues involved stating that the "...developing countries often manifest schizophrenic symptoms on the issue of private foreign participation."[28] The developing countries at the first UNCTAD

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26. UNCTAD 1989, TD/B/C.3/229, "Insurance in Developing Countries: Review of Developments in 1986-1988,"p.3.

27. The moves to liberalisation of trade in insurance services was reinforced during the Uruguay round of multilateral trade negotiations (MTN) of GATT (General Agreement on Tariffs and Trade). Former negotiations had emphasised the trade in goods, but since the Tokyo round of MTN the US as well as the OECD countries had increasingly supported negotiations on the issue of trade in services. See Skipper (1987,pp.60-61), UNCTAD TD/B/C.3/229,pp.4-5, and Carter and Dickinson (1979,pp.61-70)).

session solicited the developed countries assistance in implementing these policies. This assistance was not forthcoming as a result of which the 1972 UNCTAD resolution invited developing countries to take measures which would lead them towards the achievement of the objectives set out in the first resolution (Ripoll 1974,p.81).

The policy measures eventually adopted in this regard were;

(1) policies prohibiting or discouraging the purchase of insurance and reinsurance services from foreign insurers,

(2) the requirement that foreign companies incorporate locally, and

(3) the imposition of restrictions on the repatriation of net premium balances or net earnings of foreign insurers and reinsurers by implementing exchange control restrictions or insurance supervisory policies (Dickinson 1986,p.81).

A distinction could be made as regards the above between restrictions imposed on "establishment" (categories 2 & 3 above) and "services" (category 1 above) business. Apart from direct barriers in the form of restrictions on the purchase of insurance and reinsurance services from abroad and the imposition of exchange control regulations, inter alia, indirect barriers to the foreign supply of insurance business may exist in the form of fiscal policy, and the requirement for the localisation of reserves.

With respect to establishment business where the direct barriers may be imposed by nationalisation, indirect restrictions may include; restrictions on remittances, discriminatory capital requirements, domestication, restrictions on the employment of expatriate personnel and discriminatory market practices.[29] These policies have been criticized on the basis that, inter alia, the resultant insurance markets would be too narrow, with the consequence of increased costs to local consumers. Additionally, it has been argued that insurers seek to invest their funds in the developed country markets because the rates of return on investments in these markets are higher than

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28. Position paper on International Insurance and Reinsurance, International Insurance Advisory Council, Chamber of Commerce of the United States, Washington, D.C., 1972, in Ripolli (1974,p.80).

29. See Carter and Dickinson (1979,pp.19-33) and also Skipper (1987,pp.65-71).

those of local markets, as a result of defective policy measures in these markets which contribute to low returns (Hindley 1982).

It has also been argued that "restricting" market operations in this sense is against the very concept of insurance (Ripoll 1974,p.82), that is, the geographical spread of numerous risks by the insurance companies in order to spread the loss occasioned by a few policyholders amongst a large population of policyholders.[30] It is thought that while restrictions on the supply of foreign insurance on a services basis could reduce to a significant extent, the product choice and quality of service available to the large industrial and commercial purchasers of insurance, individuals and small businesses are affected to a lower degree. The argument is that the needs of the latter are usually unsophisticated and can be supplied by domestic insurance companies,[31] while the former usually require in addition to insurance cover, specialised loss prevention, engineering and risk management services that domestic insurers may not be able to supply (Carter and Dickinson 1979,pp.34-38).[32]

With respect to the supply of life insurance business, foreign insurers are also said to bring the following benefits (1) experience (that is highly skilled foreign personnel, advanced technology and a knowledge base that can be transferred to the "national work force") (2) capacity (cost efficient creation and marketing) (3) competition and (4) increased revenues to host developing countries largely through the taxation of foreign life insurers and licensing fees (Greenberg 1986,pp.31-32).

The argument that the purchase of foreign insurance services is a strain on developing markets balance of payments position has been criticised on the basis that the net flow of insurance funds between any two countries is probably substantially smaller than the gross flows. Though gross flows may at first impression appear to be large, the net flows are said to be very small when compared with other items in the balance of payments accounts or GNP of the country. The figure is usually less than 3%, with the exception of the UK (Wasow 1982,p.89; Carter and Dickinson 1978,pp.16-17). Apart from this it is also argued that although fiscal or other policy measures implemented might result in a reduction in deficits on the current account, the size of the reduction depends on the ability of the local insurance market to meet the local demand for

30. See generally, Athearn 1977, Bickelhaupt 1979 and Mehr and Cammack 1976.

31. Carter and Dickinson argue that this holds true more so with respect to life insurance business since consumers in any case prefer to purchase insurance services from local companies rather than foreign companies.

insurance. This ability is usually impaired because of capital shortages and the lack of managerial expertise so that eventually the local demand is passed onto international reinsurance markets (Dickinson 1986,p.81).[33]

However another factor has to be taken into consideration. Because the insurance portfolios of developing countries are usually small, the operation of the law of large numbers[34] is often impaired so that reinsurance is increasingly used as a means of reducing portfolio risk. Third world insurers characteristically over-reinsure because of the lack of reinsurance expertise, their small and uneven portfolios and the temptation to receive insurance commissions. Consequently the outward flow of reinsurance premiums in developing countries does not bear a relationship to the local reinsurance protection needs. There appears to be sufficient justification for this argument. UNCTAD[35] noted that the demand for reinsurance in many developing countries was steadily increasing, despite the reduction in economic activities in these countries. The situation is compounded because international reinsurers not only fix the price for the reinsurance services they render, but also dictate to some extent the terms and conditions under the contract as evidenced by their use of "revision"[36] and "stability clauses".[37] Such premiums are based on the reinsurers global results and do not take into consideration the experience of the ceding country. As a result, "The balance of power in reinsurance transactions is thus constantly in favour of the reinsurer"(El-Hassan 1981,pp.25-31).[38] It is however argued that the imposition of localisation restrictions on premium balances on foreign reinsurers directly increases

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32. See also UNCTAD 1982, TD/B/C.3/178, "Insurance in Developing Countries, Developments in 1980-1981,p.27."

33. Mr. J.O. Irukwu, the Managing Director of the Nigeria Reinsurance Corporation, commented in an address to AIRMIC International Insurance Conference held in Paris in 1982, that "... Risks [were] getting more complex and difficult to handle..[there was] [a]cute shortage of experienced qualified personnel [and] [l]ack of expertise in the various supporting services..." in UNCTAD,TD/B/C.3/178, ibid. p.27.

34. This is a mathematical principle also referred to as "The Law of Great Numbers" or "The Law of Averages". Simply put, it states that as the number of exposures (to loss) increases, the more nearly will the actual results obtained approach probable results expected with an infinite number of exposures (Magee 1953,pp.73-74); Mehr and Cammack 1976,pp.32-33; Athearn 1977,pp.29-30). The application of this principle to insurance means that as insurers consistently increase the number of insureds in their portfolio, their ability to forecast the number of people who will actually suffer loss increases.

35. UNCTAD TD/B/C.3/178, ibid.pp.24-27.

36. Policy, July 1971, pp.666-678 in El-Hassan (1981,p.33). Reinsurers make use of such clauses to adjust premium rates in line with inflationary trends in the developing countries.

37. Bellerose,P.R., (1980). Reinsurance For The Beginner, London: Witherby & Co.,p.48 in El-Hassan ibid.p.32.

38. See also, UNCTAD TD/B/C.3/178, ibid.p.25

their production costs which are then passed on to local reinsurers and insurers in the market (Carter and Dickinson 1979,p.42).

The unavailability and inadequacy of insurance statistics[39] about the value of reinsurance cessions in the developing countries and their effect on the balance of payments makes it difficult to assess these effects and the developed countries who possess statistics on world insurance and reinsurance transactions conceal them because in view of

> "...the sensitivity of the developing countries over the possible earnings of outside insurers in their territories it is better not to say too much bout the achievements of Britain in the sphere of invisible earnings."[40]

From this the conclusion can justifiably be drawn that some foreign reinsurers are making good profits on their activities in the third world.

It has been proposed that the relevant issue in examining this question lies in the area of the opportunity costs involved in resource allocation. The developing countries have to devise ways of rationing foreign exchange to put into uses productive to the economy. Thus the issue in question is that of making a rational economic choice between alternative foreign exchange using activities by examining the relative costs and benefits involved in each activity and not by arbitrarily excluding insurance from this sphere of economic activity. When a resource such as foreign currency is scarce, it has to be rationally allocated among productive activities. However developing country governments do not permit the markets freedom of choice. They impose policy measures designed to prevent or limit the outflow of foreign exchange by way of reinsurance transactions which, it has been argued, leads to inefficient resource allocation (Hindley 1982).[41]

For example, the probable results of setting up national reinsurance institutions with the sole purpose of protecting the balance of payments position might be that local direct insurers are forced to pay more for these services than would have been the case if they had been allowed to deal directly with foreign reinsurers (Hindley

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39. UNCTAD TD/B/C.3/178, ibid.p.27.

40. Policy Holder Insurance Journal London 11 September 1970, in Ripolli (1974) at p.78.

41. See Carter and Dickinson (1979,pp.44-54) for a discussion of this issue.

1982,p.45). Apart from this, because international reinsurance business is competitive in nature, it is sometimes the case that reinsurance balances are in favour of the ceding company despite the fact that large reinsurance premiums are ceded as in the case of proportional motor treaties (Nabolz 1986,p.49). In other words, the profitability of the domestic reinsurers portfolio has to be examined as a means of assessing the costs/benefits of these policy measures. This can be determined by examining the balance payable abroad by the domestic reinsurers over a period of several years, rather than taking a snapshot view of the gross premiums involved (Hindley 1982,p.45; Nabolz 1986,pp.48-55).

UNCTAD[42] recognised the fact that "effective skill and expertise" were a necessary requirement for the effective implementation of their recommendations on insurance in developing country markets and acknowledged the fact that this was "generally lacking" in most developing countries. They recommended the establishment of national training programmes and regional specialized training institutes to alleviate the situation. The lack of human resources in these countries was however seen as the main barrier to setting up these programmes.[43] It has been asserted that the available evidence demonstrates that foreign competition does not prevent local insurers from acquiring the requisite skills, although it is acknowledged that their presence may hinder the process of market development. It is claimed that the presence of foreign insurers could actually increase the degree of advanced technical knowledge and expertise in the local market (Skipper, 1987,p.64). It is also argued that if the effect of restricting the activities of foreign insurers is to substitute inefficient local insurers for efficient foreign insurers, then the development of the market is also hindered. The situation is however believed to be changing over the years with the establishment of local, regional and international training schools for local market personnel (Nabolz 1986,p.47).

Governments are said to pursue protectionist policies because local insurers cannot provide insurance services at a competitive price compared with foreign insurers. It is also considered that protectionist policies obscure the underlying problem which is generally that of inappropriate policy measures in the local market. The effect of these policies may be to impose costs because producer interests are served by taxing local

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42. UNCTAD TD/B/C.3/121 "Insurance Education for Developing Countries,"p.2.

43. UNCTAD TD/B/C.3/121, ibid.

policyholders, and the misallocation of resources involved may serve to hinder innovation (Hindley 1982,p.6, Skipper 1987,p.64).

Evaluating the effects of protectionist policies with respect to the growth of the insurance market will invariably lead to the conclusion that these measures are successful since in many cases, the industry's dependence on imports will decline and the market experience some growth. However there are other effects that are ignored such as increased costs of operation or changes in the quality and availability of the service, which hinders the growth of the market and ultimately affects the consumer. The benefits of protectionist policies should be viewed in terms of the associated costs of growth in the sector which costs are basically opportunity costs of the resources utilised in the market (Wasow 1986,p.91; Dickinson, 1986,pp.81-82). It is recognised that although the impact of restrictions on the operations of foreign insurers may result in a welfare loss for policyholders, such restrictions could nevertheless be justified on the basis of the possible benefits to the national economy. The supply of foreign insurance services may result in better product choices and improved quality of service to individual policyholders, but from the stand-point of the national economy, the benefits may not be so apparent. Protectionism appears to encourage inefficiency among domestic companies as the lack of foreign competition may act as a disincentive to efficiency (Carter and Dickinson 1979,pp.44-45).

Although the improved financial control resulting from the regulatory system should outweigh the costs of regulation (Mortimer 1988,p.49), this is not always the case. The restrictive regulation of the developing country markets have associated costs which cannot be overlooked or ignored in assessing the extent to which regulation has conferred benefits on the market. Goodhart (1988,pp.17-31) in examining the costs of regulation in the context of The British Financial Services Act 1986, categorised the costs associated with the establishment and implementation of regulatory institutions and measures as follows;

(1) Direct resource costs (human and physical resources) which represent an opportunity cost since they could have been used in alternative productive activities. Wasow (1986) argues that since insurance is basically human resource intensive, the opportunity costs in this area are mainly human resource costs. This is because the insurance sector utilises a large number of relatively highly paid and highly educated personnel, and because they have to be utilised more intensively to generate insurance services than other goods and services,

their productivity in terms of job generation and the generation of value added is extremely low relative to other sectors of the economy (p.99).

(2) Guaranty fund costs that is the costs of establishing a guaranty (compensation fund) for the protection of investors, (in this case policyholders) in the event of the failure of an insurance company.

(3) The risk of losing business in the event that the regulatory restrictions discourage skilled labour from home or abroad operating in the market.

(4) Increased costs of operation, reduced competition and consequently static inefficiency stemming from regulatory restrictions.

(5) The costs associated with the stifling of innovative activities which lead to dynamic inefficiency in the market.

These costs are applicable to developing country markets. and although it has been acknowledged that such costs may in practice be difficult to evaluate, (Mortimer 1988; Goodhart 1988; Duguid (1988), it is considered that such an evaluation is essential before regulatory measures are implemented (Goodhart 1988).

The "infant-industry"[44] argument has been used to justify the employment of protectionist regulation in the developing country markets, but it is argued that this may not hold if the costs of protection of the industry outweigh the benefits of protection. In addition to this, although this theory may be applied to the trade in goods, it is not certain that it could be validly or appropriately applies to services in general or insurance in particular (Skipper, 1987,p.64). Thus it is considered that the argument for government intervention in developing country markets are not tenable from the viewpoint of rational economic policy and genuine national interest (Hindley 1982 p.34).

3.4 Case Study Analysis-The Evidence

Although case study analysis of the effects of government intervention in specific insurance markets have given some insight into the probable effects of various policy

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44. The protection of a young local industry by restrictive policy measures which protect it from foreign competition. The idea is that this will enable the market to grow.

measures in insurance markets as a whole, the experience in these markets cannot be used to make sweeping generalisations from these analyses.

> "...the best use of case studies is to explore what is possible and to dismiss generalizations which prove too simple" (Wasow and Hill 1986,p.175).

The potential effects of protectionist policies have to be evaluated in the light of an individual economy's prevailing (and potential) market environment and given that this may vary considerably across different economies, the effect of the same measures in different countries may not be the same.

Skipper (1987,pp.82-83) agrees with the preceding sentiment and advocates the use of what he refers to as "[b]road temporary protective measures" in many developing country markets and believes that these measures should be gradually removed to guard against permanent protectionism which may not be in the interests of these markets.

Gorre (1986) examined the effects of the nationalisation of some of the insurance companies in the French insurance industry by comparing the premium growth, level of capital and free reserves, and taxes on profits, of joint stock companies in the nationalised sector and private sector over the period from 1963-1980. His results indicated that the nationalised sector was inferior to the private sector in terms of the parameters he had defined. This differential, he discovered was mainly due to the increased level of expenses in the nationalised sector caused mainly by the greater number of executives and middle management personnel employed in the sector. The implication was that the nationalised sector companies were being run less strictly or less efficiently than the private sector companies which is usually the case with public sector organisations.

However the analysis of the effects of nationalisation of the insurance industry in India (Wasow 1986,pp.228-239) does not indicate the same pattern. In fact it appeared that prior to nationalisation foreign insurers performed less efficiently than domestic companies. These foreign companies grew more slowly and had relatively higher expense ratios and inferior underwriting results than the domestic insurers who in turn were undercapitalised and poorly managed. Although as Wasow stated, detecting the results of nationalisation was difficult, the post- nationalised insurance industry appeared to be competently run and the records of the companies

"respectable" (p.228). However, there were indications of politicisation in the process of appointing senior level managers to the nationalised companies as well as wasteful non-price competition, while consolidation of the industry had increased the power of labour unions considerably. Additionally, the net positive effect of nationalisation on the balance of payments position appeared to be very small.

In an attempt to control the insurance industry to facilitate Tanzania's economic development, the government opted to nationalise the insurance industry. It has been argued that this process has proved beneficial to the industry[45] when compared with the "regulatory model"[46] implemented by the Sudan to achieve the same purpose. Nationalisation is thus advocated as being "...more appropriate to the needs of underdeveloped countries than a regulatory model of the Sudanese type" (El-Hassan 1981). The argument is that a regulatory code is an inadequate system to depend on in a country which is characterized by such weaknesses as

> "...deficiencies in...legislation and, in particular, low observance and enforcement; lack of obedience to rules and directives handed down to public officials...; frequent collusion of those officials with powerful persons or groups of persons whose conduct they regulate..."[47]

According to El-Hassan (pp.339-340), the regulatory code in the Sudan was drafted by foreign insurers to serve their best interests with the result that the laws were generally liberal. For example, reinsurance activities and the imposition of premium rates and policy terms was not subject to any form of regulatory control. Additionally, investment regulations were not complied with and the method of valuation of the assets and liabilities of insurance companies, upon which the determination of their solvency was based, was left to the companies to determine. This coupled with the industry's influence on the regulatory department had resulted in the regulatory agency being "...destined to remain a mere depository of annual documents primarily engaged in the peripheral issues of regulation rather than a watch-dog on the industry" (p.340).

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45. For more details, see El-Hassan (1981) at pp.245-350.

46. That is the imposition of regulatory measures on the market via an insurance code.

47. Myrdal, G., (1968), "The Soft State in Underdeveloped Countries", U.C.L.A Law Review, Vol.15, p.1120 in El-Hassan 1981,pp.338-339)

In Korea (Wasow 1986,pp.242-263), public policy in the field of insurance has been protectionist and the insurance industry has been structured to facilitate the national policy goals of economic growth and industrialisation. The government controlled pricing, so that premium rates were high and loss ratios relatively low by international standards. The absence of price competition had hindered innovative activity as in the Indian experience. Despite these limitations, the industry was growing rapidly and the costs of protectionist policy in Korea was less than would have been the case in other developing countries. This was because Korea was well endowed with skilled, educated people so that the opportunity cost in terms of human resources was expected to be low as skilled personnel could be obtained for the insurance sector without a loss to other sectors of the economy (p.249).

The Brazilian experience (Hill 1986,pp.211-239) also debunks the theory that protectionist measures are inimical to the development of an insurance industry. Here, government increased the degree of regulatory control over the market in order to generate greater retention capacity for the domestic market and to facilitate asset growth. Pursuant to this the market was consolidated and restrictions placed on the participation of foreign insurers while efforts were made to reduce the volume of insurance imports. The implementation of these measures appeared to have improved the performance of the industry in terms of increased growth rates, reduction in expenses, higher profits and increasing consumer benefits. The projected improvement in balance of payments position with respect to insurance however did not materialise as has been the case with most countries implementing the "decrease insurance imports and limit foreign participation" strategy (Wasow 1986,p.249; Hill 1986,pp.222-227).

Despite the resulting increase in the price of insurance services, the implementation of protectionist policies in the Japanese insurance market appeared to be beneficial in the wider context of the prevailing economic environment in Japan during the period under consideration (Soejima 1986,pp.250-263). The Japanese economy was a fast growing one and the insurance industry was described as one of the fastest growing markets. However it was acknowledged that with the impending reduction in economic growth, these existing policies had to be modified to take into consideration new developments in the economy.

3.5 Government Participation in The Nigerian Insurance Industry

The available literature on the Nigerian life industry in general have been mostly written by insurance industry practitioners and a few academicians who have developed an interest in the subject. Consequently, most of the work done in this area has been of a descriptive, rather than investigative or empirical nature.

Akintola-Bello (1983,p.1) in his work on the structure of the Nigerian insurance industry, commented that the existing works in the area of insurance had not been sufficiently micro-analytic, being mostly general analyses of growth trends, market shares by line of business and investment patterns. A survey of the literature confirms this assertion. Most of these works have been of a descriptive nature and very few, such as Akintola-Bello (1983), Akhile (1990) and Msheliza (1991) have involved any empirical analysis. This is not surprising if the following factors are taken into consideration:

(1) many of the papers have been written by industry practitioners who have had the tendency to produce papers which although informative have not been scholarly in approach,

(2) insurance has only recently (as late as the 1970's) become an academic subject in Nigeria's institutions of higher learning and as such the area has not been subject to much scholarly research.[48]

(3) the lack of adequate, reliable, and consistent insurance industry statistics to work with and

(4) the lack of funding for insurance based research.

The lack of formal methodical research into the industry has been frequently commented upon. Lijadu (1987,p.25) observed that the area of insurance research has been neglected. He stated that

> "...there is no institution in Nigeria today that offers post graduate courses in insurance...The success of the Nigerian Insurance Industry

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48. This trend appears to be changing. There are now two doctoral works on the Nigerian insurance industry, Falegan 1991 and Msheliza 1991.

> will almost certainly depend on research...the willingness of top managers in the industry to sponsor research ...has not been too encouraging."

Because insurance company investment behaviour and performance are essential to insurance company profitability, solvency and viability, quite a lot of work has been done in this area in the developed insurance markets such as the UK and the USA. This is not, however, the case with the Nigerian Insurance Industry. There are a few papers, notably Ogunshola (1976), looking at the investment and related problems with which Nigerian insurance companies are faced. Ogunshola's finding was that the existing regulatory framework for the investment of insurance funds was restrictive and this, coupled with the increasing inflation in the economy, was adversely affecting the performance of the funds. This is consistent with the arguments in Falegan (1976).

Falegan (1982) examined the regulatory framework for the investment of insurance funds. In his appraisal of the effectiveness of the use of the portfolio ceiling device and the regulation of interest rate method policy instruments as regulatory measures, he concluded that these measures led to "...less efficient markets, imposes adverse distributional effects and distorts relative factor prices between sectors" (Falegan 1982(d)).

In his study on the economic contribution of the insurance industry in Nigeria's economy, Akintola-Bello (1985) tentatively concluded that the predominance of very small but non-specialist firms could affect the investment and claims performance of the industry and stressed the need to extend regulation to improve investment quality. Agu (1986) came to a similar conclusion in his assessment of the actual and potential contribution of the insurance industry to the nation's economic development. He stated that the investment pattern of insurance companies "should be a matter of concern to the economy" and believed, like Ogunshola (1976) and Falegan (1982(d),) that the unattractiveness of the investment opportunities available to the insurance companies was as a consequence of the implementation of the monetary authorities public policy measures.

Akhile's (1990), empirical study into the interrelationships between insurer size, ownership and labour efficiency in non-life insurance business suggests that insurers with some degree of foreign capital ownership were more efficient (in terms of the generation of premium income relative to the size of labour force) than their fully

indigenous counterparts, while the larger insurers (in terms of asset base) were relatively less efficient in generating premium income. Since the study was limited non-life business, the conclusions reached cannot be properly extended to the life market.

Msheliza's (1991) examination of the strategic planning in the Nigerian insurance industry yielded results that suggest, among other things, that the government owned insurance companies are less involved in strategic planning than the other companies in the industry. In addition to this, empirical analysis appeared to suggest that there was evidence of economies of scale in non-life but not life insurance business, that there was evidence of price competition in life insurance, and that there were economies of scale in respect of management expenses (p.223). Msheliza's analysis also suggested that medium size companies have lower cost structures and higher profits than the small and large companies which implies the existence of minimum efficient scale. His analysis was however, limited to a 1984 cross-sectional study of the companies concerned.

A detailed examination of the role, nature and effectiveness of government intervention in the Nigerian insurance industry was carried out by Falegan (1991). The study is descriptive. His conclusion, among other things, was that the apparent benefits of the protectionist measures implemented by the government were more apparent than real because these policies had resulted in increased transaction costs and market frictions (p.319). His conclusions were based on a theoretical analysis of regulatory provisions, and a survey of the perceptions and opinions of insurance company executives as to the relevance and effectiveness of these regulations and their impact on industry structure, conduct and performance. On specific issues such as governments participation in the industry, Falegan argued that this had resulted in market concentration, with a resultant welfare loss[49] to consumers in terms of the increased prices they had to pay for insurance services. He also stated that the country's balance of payments position in respect of insurance services was not showing any improvement since domestic reinsurers were retroceding a large portion of the risks which had resulted in an outward flow of foreign exchange (pp.227&307).[50] In addition, he described the insurance market as being oligopolistic while like Msheliza (1991), he said life insurance, "...readily responds to competition

49. Falegan did not attempt to measure the extent of the welfare loss.

50. See Falegan 1986 for a general discussion of the effects of localisation policy on the Nigerian insurance market.

[because there was]...no restriction on [it's]...supply other than it's fiduciary regulation" (p.315).

In the study he hypothesized that "...although established insurers tend to favour market discipline, they do not want regulation for it's own sake but only if they can profit by it" (p.325). Falegan attempted to determine if this was true by interpretation of the responses to some questions on regulatory provisions by means of an administered questionnaire. He analysed the responses by classifying them according to the ownership pattern of the insurance companies, joint venture,[51] state owned and private domestic. His results appeared to confirm the hypothesis. Falegan concluded that the joint venture firms were not averse to capital requirement and licensing provisions since they, by virtue of their size were able to absorb the costs of regulation (p.324). He concluded that based on these factors government should focus on the development of the capital intensive sectors of the economy and leave the insurance sector to private interests.

Falegan's study was the first comprehensive investigation into the effect of government intervention on the activities of insurers. His conclusions are significant with respect to the study at hand, but most of them were arrived at without any rigourous empirical analysis. Furthermore the study was a general analysis of the whole insurance market and does not treat the life market specifically. The insurance product is however heterogeneous across the various classifications of insurance business and for an effective analysis of the industry, the main lines of business have to be analysed separately.

Summary

The demand for insurance is positively correlated with the rate of economic development. As a result, government policy in the insurance market in developing country insurance markets is geared towards, not only policyholder protection, but on implementing measures that will stimulate the growth of the market. The objective of policy is to strengthen the market by increasing retention capacity and reducing the reliance upon the importation of insurance services. Thus many developing economies implement protectionist policies of various kinds in order to co-ordinate

51. The term includes domestic (local) subsidiaries of foreign insurance companies and companies with part government and part domestic ownership.

the activities of insurers with national development objectives. It is argued in some quarters that these policies do not benefit the developing economy markets in the long run, and many western economists and insurers object to their implementation. At the opposing end are the protagonists of protectionist policies who argue that the developed countries objectives are simply to control the premiums and profits in third world markets, as an extension of past colonial interferences in such markets.

Although the evidence from case study analysis generally appears to favour the imposition of protectionist policies in such markets, sweeping generalisations cannot be made. The economic conditions and structural characteristics of individual markets has to be taken into account in determining the policies best suited to each country, and the potential costs and benefits of regulatory interventions have to be taken into consideration in the determination of public policy.

The Nigerian life industry has not been the subject of much scholarly research. However, the evidence from available studies suggests that the market is price competitive, and there are no indications of the existence of economies of scale. Government intervention in the life market is said to have restricted investment choice. No attempt has been made to study the relative efficiency between the different categories of companies operating in the market.

In the next chapter the political economy of Nigeria is discussed first, to form a basis for the analysis of both regulatory developments[52] and industry structure, conduct and performance.[53]

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52. Discussed in chapter 5.

53. Discussed in chapter 6.

Chapter 4

The Political Economy of Nigeria

Introduction

In order to facilitate the discussion on the political economy of Nigeria, the developments in the country from colonial times up till the present will be examined in three phases. First, a brief excursion will be made into the colonial background of the country up till independence in 1960. Then the post-colonial era will be examined in three phases, the Agrarian Period, the "Oil Boom" period and the Period of Economic Recession.

Nigeria is located on the West coast of Africa and has an area of 356,669 square miles, about four times the size of the United Kingdom. It lies approximately between 3o and 15oE longitude and between 4o and 14oN latitude and is bordered to the west by the Republics of Benin[1] and Niger, to the east by the Cameroons, northwards by the Niger and Chad Republics and to the south by the Gulf of Guinea[2] (Ekundare 1973,p.5). The capital is Lagos, in the southern coastal region.[3]

Nigeria is a tropical country and physical conditions vary within the country. The northern part of the country is dry and sandy, while the coastal region is damp and swampy. The seasons are delineated by a dry season which begins in the northern parts in October, ending in April. The dry season is characterised by the harmattan, a dry north-easterly cold wind. In the south the dry season is of a shorter duration, lasting from about November to March (Burns 1972,p.23; Ekundare 1973,p.5). The country's population is 105.2 million,[4] 1989 figures[5], and per capita income is estimated at $250, 1991 figures.[6] The country is currently divided into 31 states,

1. Formerly Dahomey Republic.

2. This includes the Bights of Benin and Biafra.

3. The capital city is in the process of being transferred to the Federal Capital Territory in Abuja.

4. Nigeria is believed to be the most populous country in Africa. It is estimated that one in every four Africans is a Nigerian.

inclusive of the Federal Capital Territory of Abuja. Although the lingua franca is English, Nigeria is a multi-lingual and multi-cultural society (there are over 250 ethnic groups in the country)[7] and the two predominant religious groups are the Christians and the Moslems. A proportion of the population practice some form of African traditional religious practices. Nigeria has been under military rule since 1983, although it is currently in the transition process to civil rule.

4.1 The Colonial Era

Nigeria was created by the amalgamation of the two British protectorates of Northern and Southern Nigeria in 1914. The country had become a British protectorate in 1865, when the British in a reversal of their averred policy on colonialism claimed a protectorate over the Niger Districts.[8] The country had a thriving export trade in cocoa, palm oil and palm kernels (from the southern part of the country) and groundnuts and cotton, which came from the north, and the British saw no sense in continuing trade agreements with the "natives" when they could take over the factors of production. Agriculture accounted for almost two-thirds of the country's gross domestic product.

Foreign firms had considerable commercial operations in the country and some of them established manufacturing enterprises.[9] This was actively encouraged by incentives and inducements to attract foreign capital. In the period between October 1946 and March 1958, 1,027 foreign companies were registered in the country, a considerable increase from the 182 that were registered in the previous decade (Akinsanya 1983,p.149). At this time although an industrial policy was designed for the country, the policy measures were primarily in the form of import duty and tax reliefs geared towards facilitating the trading activities of the foreign companies in the market. The Colonial Government had never had the intention of industrialising the economy since Nigeria was supposed to be a trading post from which raw materials were extracted to the metropolitan capital and other overseas markets, and to which finished goods could be exported without hindrance. As a consequence of the high

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5. IMF International Statistics Year-book 1991,p.571.

6. Financial Times Survey on Nigeria, Monday March 16, 1992,p.I.

7. Lloyd's Bank Ltd. Overseas Dept., 1976, Economic Report on Nigeria.

8. Reference sources on the history of Nigeria include Crowder, M., (1978), The Story of Nigeria, London: Faber and Faber, and Burns, A., (1969), History of Nigeria, London: George Allen and Unwin.

level of foreign capital in the country, government control of the industrial sector at this stage of the country's development was minimal (Teriba and Kayode 1977,p.322,330).

The first attempt of the British to "plan" the Nigerian economy was in 1945, when the "Ten-Year Plan of Development and Welfare for Nigeria 1946" was designed. The plan was revised in 1951 to cover the 1951-1956 period. The plans were however not considered to be plans in the true sense of the word since they were not co-ordinated or related to any single economic target. The International Bank designed another plan in 1955 to cover the 1955-1960 period, but it was not till after independence that serious attempts were made at co-ordinated planning in the country.[10]

4.2 The Post-Colonial Era

4.2.1 The Agrarian Economy 1961-1970

Following the rise of nationalist sentiments and the associated political upheavals, the British relinquished their political rights over Nigeria in a peaceful transfer of power in 1960. Subsequently successive post-colonial governments in power designed development plans which were aimed at "shaping the design of [the] nations economic development," and one of the objectives of development planning was to give the country "an increasing measure of control over her own destiny."[11] The ultimate objective of development planning was to develop the Nigerian economy to the point where it would become increasingly independent so that it's reliance on foreign capital and technical assistance would be reduced.

Before independence, Nigeria's industrial life had been dominated by the export of raw agricultural products, with agriculture accounting for 56.7% of GDP. Thus the first National Development Plan[12] document accorded "the highest priority to agriculture, industry and technical education" and it's major objective was to maintain an average growth rate of 4% per year in the country's GDP. This was to be attained

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9. See The Economic Development of Nigeria, 1955, Baltimore: The John Hopkins Press

10. Federation of Nigeria, National Development Plan 1962-1968, pp.6-7.

11. Federation of Nigeria, National Development Plan 1962-1968,pp.2-3.

12. Federation of Nigeria, Federal Government Development Programme 1962-1968, Sessional Report No.1 of 1962, and National Development Plan 1962-1968,p.23.

through the investment of approximately 15% of GNP per year into the "directly productive sectors of the economy." The government aimed to stimulate the growth of the industrial sector by encouraging and stimulating growth in the private sector in the economy. Although the desirability of encouraging a high level of indigenous participation in the economy was recognised, it was however realised that in order to achieve the desired growth "A substantial amount of foreign assistance and capital imports" would be required. Government policy at this time was one of limited participation in enterprise, and it focused it's attention on the development of infrastructure in the economy. The National Plan document described the Nigerian economy as a mixed economy[13] and although the public utilities, shipping, airways, railways, power, communications and marketing boards were nationalised, government leaders indicated that there were no plans to nationalise industry beyond these measures. As far back as 1952, the Minister of Commerce and Industries, A.C Nwapa, had declared,

> "You must realise what government can do and what it cannot do. Industry is a purely commercial enterprise...The Government's responsibility is to provide communications, power, social services-those are the things which fall rightly within the province of Government, but a shoe factory, an umbrella factory-No-that is too much to ask of Government (Blunt 1977,p.81).

In 1956, his successor, R.A Njoku also spoke in the same vein;

> "The Government has to evolve a policy of industrialization. We do not believe that all the industries should be started by the Government and should be controlled by the Government. The Government's work is to help companies, corporations and private people to establish their industries, and experience has shown that where the Government has engaged in industry the whole thing could not be run on a commercial basis" (Blunt 1977,p.81).

The Government's intentions were specified in the first National Development Plan document. However the lack of domestic and foreign capital and expertise was an obstacle to the successful implementation of Governments industrial policy and the necessity of foreign capital was acknowledged. However from the start the possibility of the Nigerianisation of foreign interests in the economy was indicated. Sir Abubakar Tafawa Balewa the country's first Prime Minister, in a parliamentary speech stated that

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13. National Development Plan 1962-1968,p.21.

> "It must be obvious that no Nigerian can be content so long as any major sector of the economy is controlled by foreigners. But we are realists and we say that so long as there is a dearth of Nigerian capital, so long must there be an opportunity for foreign capital in Nigeria. We do not seek the withdrawal of foreign capital from any area of the economy before Nigerian enterprise is able to replace it. When the time for withdrawal has come, due notice will be given (Proehl in Akinsanya 1983,p.146)

The Government also promised that when the time came for the "withdrawal" of foreign capital, adequate compensation would be paid, and this was provided for in the provisions of section 30(1) of the Nigerian Constitution (Akinsanya 1983,p.146,147). The Governments policy was therefore to encourage direct foreign participation in the industrial base of the economy while indigenous businessmen were encouraged to move into areas where they had some expertise such as retail, semi-wholesale and service activities, among others. These local entrepreneurs were, however, faced with many problems. In addition to shortages in capital and entrepreneurial capacity, there were obstacles/difficulties in the economic environment. These came in the form of capital equipment and [skilled] human resource problems, problems encountered in the procurement of raw materials and intermediate goods, as well as infrastructural problems among others. The foreign investors, unlike their indigenous counterparts, were not hindered by most of these difficulties. They had large capital bases, skilled personnel, and overseas links which did much to facilitate the conduct of their business operations in the country (Schatz 1977,pp.35-46).

The Governments policy stance towards foreign investment had been taken as far back as 1952, before the country's independence. In order to encourage foreign investment in industrial activity, some industries were designated as "pioneer industries" and companies investing in them were given, among other things, tax holidays for a period of between two to five years depending on the levels of investment made. During the succeeding years more liberal legislation and economic inducements directed towards this were implemented.

There was some opposition in some quarters to this strategy. The Leader of the Opposition in the House of Representatives, the late Chief Obafemi Awolowo, in 1960 was of the opinion that although foreign investors should be encouraged, Nigeria should say "in effect to foreign investors `come to our aid in the meantime but in due course we will buy you out" (Phillips in Akinsanya 1983,p.150). This statement led key political figures at home and abroad to make statements clarifying

the Governments stance on this issue. Dr Michael Okpara, the then Premier of the former Eastern Nigeria, referred to Chief Awolowo as a communist stating that "Those who are advocating nationalization are communists and should have the moral courage to say so" (Blunt 1977,p.82).

The debate on nationalisation continued. Chief Awolowo advocated the nationalisation of the insurance, mining and merchant marine businesses among others, on the basis that, among other things, nationalisation was essential to the successful development of the nation. Chief Okotie-Eboh, the Federal Finance Minister and the Leader of the Government Business in the Federal Parliament firmly opposed such measures. He had earlier noted that it "was most distressing" that "people who should know better are propounding new and dangerous philosophies" which include "loose talk of Nigeria being in the pocket of Britain, economically, politically and otherwise, and talk of nationalisation". He gave a warning that such talk would only serve to frighten off foreign investors at a time when foreign capital and foreign technical assistance and expertise was so badly required. One of the ministers objections to nationalisation was the experience of the existing statutory corporations which he said almost all paid exorbitant salaries and were not properly managed. The minister stated that he was not opposed to nationalisation in principle, but believed that it was not in the interests of the Nigerian populace at that point in time. He however conceded that there could be some circumstances in which nationalisation could be possible, for instance if foreign participation was not desired and indigenous capital was inadequate or not forthcoming. Thus Government policy towards state intervention in industry was one of opposition to such intervention except where the intervention was in the public interest or for national security or economic development (Blunt 1977,p.82, Akinsanya 1983,pp.150-156).

The fears of those advocating a policy of nationalisation of industry were expressed in a speech by the Opposition Chief Whip, Chief Akin-Olugbade, who after denouncing the "imperialist exploiters" concluded that there was

> "...no need to nationalise if the economy of our country is in the hand of indigenous Nigerians...if we fail to act, and to act quickly, the chances for our economic survival will be made more remote" (Blunt 1977,p.85).

This period in Nigeria's political history was a turbulent one. Ethnic and regional rivalry had resulted in political disturbances and since independence, there had been friction between the tribes in the country. The Ibos in the east were becoming increasingly fearful of being dominated by the powerful northern Hausas/Fulani.

There were violent clashes and disturbances between the various ethnic factions in the regions. Ultimately, after a bloody coup in January 1966, the army intervened and Major-General Aguyi Ironsi became the nations leader. His leadership was shortlived however. His attempt to impose unitary rule led to a counter coup and General Yakubu Gowon became the new leader of the federation. In order to remove the fear of domination by the northern region, the country was divided into twelve states in 1966.[14] The ethnic rivalry and political disturbances still continued, however, and on the 30th of May 1967, the Eastern region of the country (led by Colonel Odumegwu Ojukwu) seceded and declared an independent "Republic of Biafra". This move was firmly resisted by the Federal Military Government and thus began the Biafran war, a bloody bitter civil war which lasted until January 1970.

4.2.2 The Oil Economy 1971-1979

The Second National Development Plan was launched in 1970, after the end of the civil war. The plan was developed for the five year period from 1970-1974, but was later extended to March 1975. New policy goals were set in keeping with the governments plans of reconciliation, reconstruction, rehabilitation of the economy. Thus the main objectives of the plan were stated as the establishment of

(1) a united, strong and self-reliant nation

(2) a great and dynamic economy

(3) a just and egalitarian society

(4) a land of bright and full opportunities for all citizens

(5) a free and democratic society.[15]

Following the change in the political power base of the country from civilian to military rule, there was a marked shift in the Governments industrial policy. The increasing dominance of foreign business in many sectors of the Nigerian economy was a matter of concern for the Federal Military Government and this initiated a

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14. The country was further divided into nineteen states under General Mohammed's rule.

15. Federal Republic of Nigeria, Second National Development plan 1970-1974,p.32.

change in government policy towards foreign investment. In the Second Plan, the Government had stated that it would

> "... seek to acquire, by law of necessity, equity participation in a number of strategic industries that will be specified from time to time. In order to ensure that the economic destiny of Nigeria is determined by Nigerians themselves, The Government will seek to widen and intensify its positive participation in industrial development."[16]

The Government subsequently identified a number of "strategic" industries in which it decided to invest. The strategic industries were defined as those which were of national significance and in which private indigenous capital might be unavailable or inadequate. Even where such capital was forthcoming, the Government decided to invest in certain industries for reasons of economic nationalism, among others. The Governments ownership and control of strategic industries was aimed at maximising the local retention of profits, increasing the industrial contribution to the economy (Ogunpola 1977,p.310).

This was the genesis of active government intervention and participation in the economy. A number of control measures were implemented pursuant to the Military Governments industrialisation policy. Some of these controls were physical, financial and managerial in nature. In 1968, the Companies Decree 1968 was promulgated. This decree made regulatory provision for the formation and operation of businesses in the country, and made it compulsory for foreign companies to incorporate locally in the country. Regulations were made requiring that import licenses be obtained for the importation of specific goods into the country, and in 1970, in an unsuccessful effort to mitigate the rising inflation in the country, the Price Control Decree was passed. The decree established a Price Control Board to set prices at which commodities could be sold, and banned the hoarding of such goods. The proliferation in the number of mushroom banks prompted the promulgation of the 1969 Banking Decree which regulated bank paid-up capital and statutory reserves. There were also controls on immigration and foreign exchange imposed on the country.[17]

Apart from considerations of Nigerianisation of the economy, there appeared to be other motivating factors behind the Government's policy towards foreign capital. It has been suggested that mounting pressure was put on the government by indigenous businessmen of the bourgeoisie class who wanted "a protected niche in the economy

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16. Second National Development Plan,p.289.

free from foreign competition and a share of the proceeds of the most successful (foreign dominated) sectors of the economy." Their desires were compatible with that of the ruling military elite who were said to have become "increasingly distrustful" of foreign capital (Biersteker 1983), and in February 1972 the Military Government promulgated the Nigerian Enterprises Promotion Decree 1972, which came into effect in April 1974. This was the first indigenisation decree which was aimed at increasing the participation of Nigerians in economic activities in the country. The decree banned foreign participation in 22 types of business activity,[18] which included advertising and public relations, forwarding and clearing agencies, bread making and the retail trade among others. These business activities were classified as schedule I enterprises and were exclusively reserved for Nigerians. Schedule II businesses consisted of business activities in which foreigners could participate provided that Nigerians held a minimum of 40% of the equity capital of such businesses.

In addition to this the Government acquired equity interests in petroleum production and petroleum distribution (55% and 60% respectively), and nationalised Esso Standard Ltd. Before this time the Government had refrained from making direct investment in the mining and extraction industries because of the technology and extensive capital outlay required (Ogunpola 1977,p.311). As a result the extractive industry was dominated by foreign capital, for example, Shell-BP (British), Agip/Phillips (Italian/American), Mobil Oil (American) and Elf Oil (French).

The Nigerian Industrial Development Bank, Nigerian Bank for Commerce and Industry and the Nigerian Agricultural Development Bank were also established to provide credit facilities for Nigerian businessmen who desired to take advantage of the business opportunities created by the provisions of the decree (Akinsanya 1983,p.161,171). The government also invested 55% in the iron and steel and fertilizer production. This was the era of the oil boom and the government had the requisite funds to undertake these policy initiatives. At a point during this period, in a speech on national television General Gowon stated that Nigeria's problem was not lack of money, but how to spend it. The country, the Government and the governed alike were on a spending spree which would have terrible consequences.

Government spending went on relentlessly and unabated. The Governments budgetary expenditures were rapidly exceeding oil revenues and the oil revenues were

17. See Teriba and Kayode 1977 and Akisanya 1983 for discussion of these control measures.

18. See schedule 1 of The Nigerian Enterprises Promotion Decree 1972.

not being utilised to develop the economic infrastructure. Thus although the economy was experiencing rising growth in GDP, it was not developing (Sadri and Williamson 1989). The Gowon government launched the Third National Development Plan 1975-1980, which was aimed at using the country's oil wealth to extensively transform the economy, socially, physically and in terms of infrastructure. The plan was ambitious and priority was given to the development of industry and agriculture. Although the agricultural sector employed about 70% of the population, its contribution to foreign exchange earnings had fallen from 80% (pre oil boom era) to 10%.[19]

In July 1975, after 13 years in power, General Gowon was displaced in a military coup and was succeeded by General Murtala Mohammed. There had been increasing dissatisfaction with his government with regard to the way in which oil revenues were being disbursed. General Mohammed's short leadership was marked by a series of radical changes. He commenced a programme of "War Against Indiscipline" that covered almost all aspects of socio-economic life.[20] There were mass dismissals of public servants and military personnel in an attempt to rid Nigerian society of the general laxity and indolent work attitudes that had characterised the public sector, which had become a lumbering bureaucratic machine. It was at this time that one of the most important amendments to the Nigerian Enterprises Promotion Decree was made (the 1972 decree had been amended and updated in 1973, 1974, 1975 (Ake 1985), after the Federal Military Government appointed an industrial enterprises panel in 1975 (Aliko 1976), to examine and review the provisions of the Nigerian Enterprises Promotion Decree. The purpose was to reassess the extent of foreign investment in the country in order to increase the extent of local participation in medium and large sized firms. At this time, the amount of U.K and U.S investments in Nigeria were estimated at about £800 million and US$1,0000 million.[21]

In February 1976, General Mohammed was assassinated in a "bloody" coup attempt and General Olusegun Obasanjo, with "great reluctance" assumed the leadership of the nation. The military fervour with which the late General Mohammed implemented decisions continued under the new leadership albeit to a lower degree. The industrial enterprises panel at this time made recommendations to the Government, under which

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19. Lloyd's Bank Ltd.,1976, op.cit.

20. For example, the government imposed the "queuing culture" on the populace. Nigerians are not known for their patience.

21. Figures obtained from ABECOR (Barclays) Country Report on Nigeria, 17th May 1976.

all businesses were classified into three schedules. The result of this effort was the 1977 Nigerian Enterprises Promotion Decree. As with the earlier decree, schedule I enterprises were the exclusive preserve of Nigerians, while Schedule II contained a list of 57 enterprises in which the equity participation of Nigerians could not fall below a minimum of 60%. This included banks and insurance companies. Schedule III covered all businesses not otherwise classified in which the minimum equity participation was stipulated at 40%. Thus "Nigerianisation" of the Nigerian economy became the basis of the country's industrial policy.

This policy however merely produced cosmetic changes in the economy. Although ownership had changed, indigenous representation at the managerial level did not increase appreciably. Many reasons have been adduced for this, among which are, the shortage of skilled manpower in the economy, the efforts of foreign investors (aided by some Nigerians) to frustrate the indigenisation effort,[22] and the fact that the equity interest of Nigerians in many companies was weak because of it's atomistic nature (Akinsanya 1983,p.178-179). Apart from this the 1977 decree in section 7 made allowance for continuing foreign ownership in business enterprise under specified conditions, and as such encouraged foreign ownership and control of the economy. In addition to this the indigenisation exercise simply served to transfer the wealth into the hand of some privileged indigenous businessmen and bureaucrats (the national bourgeoisie) who were thus able to assimilate themselves into Nigeria's capitalist class. These people supported and co-operated with the policies of their colonial mentors which served their self interest (Williams 1976,p.33, Obasi 1988). In the financial sector, foreign minority shareholders were able to stymie the indigenisation efforts to some extent by the use of weighted voting shares[23] and through manipulating the technical and service agreements between the institutions and their foreign partners. This resulted in a situation where the economic surplus from the country's banks and insurance companies was (as in the colonial era) still being extracted to the metropole (Obasi 1988; Agu 1989,p.8).

Agricultural and industrial output in the economy were depressed for most of 1975, and food shortages were a problem. The Government earmarked ₦63 million for the importation of foodstuffs to relieve the shortages. Inflation had accelerated, from 14% in 1974 to 43% in 1975. Among the factors responsible for this were a high level of aggregate demand in the economy coupled with an inadequate supply of domestic and foreign goods. The Government was concerned about the growing inflationary trend

22. See Biersteker (1983,pp.192-205), for the various ways in which this has been accomplished.

in the economy and set up an Anti-inflation Task Force to examine the issue.[24] In order to stimulate production in the neglected agricultural sector, the government introduced some measures such as tax incentives for investments in agriculture and processing, and the removal of import duties on raw materials for livestock feeds among other things. Preferential interest rates were also allowed for investments into the "preferred" sectors of the economy. In the insurance sector, minimum and maximum ceilings were placed on the proportion of insurance company funds to be invested in specified sectors in the economy.[25] In addition to this, the rates of interest on insurance company loans to specific sectors were brought under the regulatory rules of the Central Bank. These measures however had only a limited success.[26]

4.23 The Recession 1980-date

In 1979, the Military Government as they had promised under the Obasanjo regime, handed power over to the civilians, and on the 1st of October 1979, after a certain amount of public debate and controversy, Alhaji Shehu Shagari was sworn in as the country's President. During the Shagari administration, the Fourth National Development Plan (1981-1985) was launched. The focus of this plan was the achievement of self-sufficiency in food production and the consolidation and diversification of the economy so as to reduce the reliance on petroleum as the main source of revenue. This was necessary in view of the fact that as a consequence of the world-wide oil glut, Nigerian crude oil production had slumped by two-thirds. The country was in a delicate economic situation. Although there was a balance of payment surplus, the country was, and still is, dependent upon petroleum which accounted for over 90% of exports, 80% of government revenue and 25% of the Gross Domestic Product.[27]

The Shagari administration was the subject of many allegations of fraud and mismanagement of public funds. Ethnic and regional differences in the country contributed to the tension among various groups in the country. Nepotism and tribalism were rife in the country. The deterioration in the economic and political

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23. The foreign shareholdings were weighted in order to increase foreign voting power.

24. Barclays Country Report on Nigeria 17th May 1976.

25. This is examined in some detail in sections 5.2.2.1.2 and 5.2.2.2.4 in chapter 5.

26. For an analysis of the effects of these policy measures on insurance company investment income, see Falegan 1982(d).

situation led to the military seizing power once again in December 1983, when Major-General Buhari came to power. The new military government was reformist in character and introduced sweeping changes in the socio-economic structure of the economy. Austerity measures were introduced in the form of curbs on domestic expenditure and imports, foreign exchange restrictions, limitations on overseas borrowing and a wage freeze among others.[28] The austerity measures did not however affect government spending, and "it appeared that there was [a] separate rule for government spending and this was unaffected by...austerity" (Sadri and Williamson 1989,p.6).

The Government continued negotiations with the IMF and World Bank for an IMF U.S $2-$3 billion extended facility, $300 million structural adjustment loan, and the refinancing of the estimated U.S$2-$3 billion the Government owed to export credit agencies. The loan would involve the devaluation of the Naira, liberalisation of import controls and the relaxation of petroleum subsidies. The negotiations had commenced when the country was under civilian rule, but the Shagari administration had been unwilling, in the interests of political expediency, to submit to the harsh conditionalities that came with the IMF package.

The Buhari regime became increasingly repressive in nature. There was general dissatisfaction with the increasing levels of unemployment and inflation as well the scarcity of essential commodities. The government however did not tolerate any form of criticism although it was obvious that the "Austerity Measures" it was implementing were causing a lot of economic hardship to the majority of the populace. These issues among others, led to the August 1985 bloodless coup in which General Ibrahim Babanginda came to power. The Babangida government implemented the two-tier foreign exchange rate system which was in effect a devaluation of the Naira. In addition to this, restrictive fiscal and monetary policies were implemented in an effort to stabilise the economy without any success, a situation which led a former economic adviser to the government to state that

> "...As the [balance of payments] deficit grew, so did the pressure for some further administrative intervention. New regulations-commercial and monetary-had to be put in place to buttress the existing machineries for control...new tariff changes were announced, new bans on imports were promulgated, all in the name of protecting local

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27. Barclays Country Report October 1981.

28. ABECOR Country Report November 1984.

> industries. It was clear that the economy was being choked to death by massive regulations administered by a corps of bureaucrats whose interests could not be regarded as identical with those of the businesses they were seeking to protect" (Okigbo 1988,p.8)

In 1985, the self styled "President" launched a "national debate" on the question of whether the IMF loan should be accepted or rejected. This proved to be a farce, for although public opinion was fiercely against accepting the loan, in view of the potential economic impact on the economy,[29] in 1986 the Government accepted a World Bank approved $425 million structural adjustment loan. Thus the country continued to remain largely dependent upon foreign technology and capital. This dependency is considered to have led to a number of structural problems such as the excessive dependence on manufactured imports, the inability of the domestic economy to satisfy both production and consumption needs and a weak balance of payments position among other things (Obasi 1988).

The structural adjustment programme or SAP as it came to be called, was intended among other things:

(1) to restructure and diversify the productive base of the economy in order to reduce dependence of the economy on imports,

(2) to achieve fiscal and balance of payments viability,

(3) to lay the basis for sustained non-inflationary growth in the economy, and

(4) to limit the degree of unproductive investment in the public sector and intensify growth in the private sector.

These policies were to be achieved by, among, other things;

(1) the introduction of the Second-Tier Foreign Exchange Market (SFEM) in order to achieve a realistic level for the Naira,

(2) the adoption of trade and payments liberalisation policies,

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29. For a discussion of the economic and political implications of the acceptance/non-acceptance of the loan, see Olashore 1988. Olashore argued that although the loan would definitely cause economic dislocations, there appeared to be no feasible alternatives to the conditionalities attached to it.

(3) deregulation of the economy and,

(4) the removal of government subsidies on public goods and services.[30]

In August 1987, the Government in an attempt to increase the volume of savings in the economy, announced the deregulation of interest rates[31] in the economy and in 1988, the termination /suspension of SAP. Measures to deregulate the economy were implemented. The Government as part of these measures promulgated the Privatisation and Commercialisation Decree 1988 by which it made known it's intention to divest itself of many of its investments in the public sector. The Government's rationale for this move was stated as follows;

> "The public enterprise sector...in Nigeria is quite large, comprising at the federal level alone about 100 enterprises...Government investment in this sector is over ₦23 billion (₦8 billion in equity and ₦15 billion in loans) but the returns thereon are less than ₦500 million annually. The Government is thus clearly not receiving a fair return on it's investment outlay, while it continues to pay interest charges and principal on huge loans...This state of affairs will no longer be allowed to continue."[32]

Schedule I Enterprises included enterprises that were to be partially privatised (commercial and merchant banks; Agricultural, co-operative and development banks; oil marketing companies; steel rolling mills, among others)[33], and enterprises to be fully privatised.[34] The latter included fourteen insurance companies in which the Government held equity. Although the Government did not specify any clear cut objectives for the decree, it was viewed as an attempt not only to deregulate the market, but to encourage the rationalisation of the public sector, generate revenue for government, reduce the public sector borrowing requirement, develop the "fragile", inefficient and underdeveloped capital market[35] and diversify the ownership base of

30. For a detailed treatment of these issues and how they affect the manufacturing sector, see for example, Eleazu (1988),pp.50-56.

31. It is argued that government control over interest rate structure in Nigeria has led to a high degree of financial repression in the market (Agu 1989, Ikhide 1990). See Ikhide ibid. for the arguments for and against the deregulation of interest rates in Nigeria.

32. Section VI(53) of the Structural Adjustment Programme Package 1986.

33. Schedule 1, Part 1 of the decree.

34. Schedule 1 Part 2.

35. For the role and efficiency of the Nigerian capital market, see Nwankwo 1980; Okigbo 1981; Ojo and Adewunmi 1982; and Akinnifesi 1988 among others.

enterprises in the economy (Usman 1988). Although the Nigerian Stock Exchange had been established as a formal and specialist market as far back as 1961,[36] the majority of the instruments available for trading were government securities and shares. In addition to this the volume of trade in the securities market was low and mainly in government stocks. The returns on these stocks were quite low (especially compared with the yields on the industrial share issues) and did not reflect the inflationary trend in the economy.[37]

Despite the various policy measures taken to stimulate the economy, a lack of private indigenous capital still existed. Since the implementation of the provisions of the 1977 Nigerian Enterprises Promotion Decree, the levels of total investment as a percentage of GDP had fallen, and the Government attributed this to, among other things, insufficient foreign capital inflow and low levels of internal savings. This led the Government to backtrack on previous policy and state that it

> "...welcomes foreign capital into the manufacturing sector...[and]...Easier capital and dividend repatriation through less cumbersome procedures is a by-product of recent changes in the regulations."

The Government therefore made an amendment to the 1977 Nigerian Enterprises Promotion Decree which was amended to contain only one list of scheduled enterprises which are exclusively reserved for Nigerians. All other enterprises (with the exception of banking, insurance and petroleum prospecting and mining) were left open to 100% foreign participation subject to a minimum investment of ₦20 million. The new measures applied to new investments only.[38]

Six years after SAP was implemented, the structural deficiencies in the economy still remain. The SAP basically encouraged the growth of the country's trade surpluses with the objective of using them to service foreign debt repayments. In March 1991, Nigeria's foreign debt stood at US$33.4 million,[39] inflation[40] and unemployment[41]

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36. It was then known as the Lagos Stock Exchange.

37. See Appendix A, tables A1-A5.

38. See "Extracts From Nigeria's Industrial Policy" in Management in Nigeria, Vol.26(3), May/June 1990,pp.43-53.

39. The Financial Times, Monday March 16 1992.

40. The consumer price index rose from 105.3 in 1986 to 259.65 in 1990 (IMF Yearbook 1991).

were still rising, the Government was still excessively dependent on oil revenues which in 1992 was 96.2% of total exports, and the debt-service ratio stood at 36%.[42]

Summary

The economic and political developments in Nigeria give the appearance of a country that is politically and economically unstable. The newly independent civilian government intended to pursue an industrial policy of industrialising the economic base of the country by stimulating private investment in a mixed economy. However the lack of private domestic and foreign capital necessitated the utilisation of foreign capital and expertise. The political leaders had not realised that political independence is not synonymous with economic independence. Although the Military Government has made attempts at the Nigerianisation of the economy, the underdevelopment of the capital market, inadequate infrastructure, pervasive government interference in the economy, as well as government financial mismanagement have had deleterious economic effects.

The fact that the political structure of the country is unstable has contributed to the inadequacies in financial policy and by implication the problems in the economic system. Between the period from 1960 to 1992, Nigeria has been under democratic rule for 12 years (1960-1967;1979-1983) and military rule for 20 years (1966-1979;1983-1992). Since the period of military rule there have been five coups accompanied by changes in the military leadership, and numerous attempted coups, accompanied by an unnecessary waste of human lives.[43]

The non-permanent structure of the political leadership of the country has led to a situation in which government policy has not been consistent over the years. When coup d'etats or changes in the nature of the political base occurred, the new leadership tended to undo and/or modify the policies of the former government in power.

Thus the Governments economic policy does not appear to have been properly designed, co-ordinated and implemented. Over the past few years financial policy has

41. The official unemployment figure (1988 figures) was 7.8%, but it is estimated to have been closer to 28%. See Okigbo (1988, p.13).

42. The Financial Times op.cit.

been indirectly determined by external sources such as the IMF and World Bank. The country is presently in the transition stage from military to civilian rule. This presents uncertainties in terms of the nature of economic policy that the new civilian administration will pursue. It is within the context of these developments in the economy that the regulatory developments in the insurance industry are examined in the next chapter.

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43. Unsuccessful coup plotters are summarily executed. For a discussion ofthe ascendancy of the military into power in Nigeria, see Okediji O.A, 1989,pp.1-37.

Chapter 5

Life Insurance Regulation in Nigeria

Introduction

For a proper understanding of some of the developments in the life market during the period under review, it is necessary to examine these developments in the light of several of the legal and economic factors present in the environment. The preceding chapter looked at the economic and political developments in the Nigerian economy: this chapter examines the objectives, sources, nature and evolution of government regulation in the Nigerian insurance industry within the context of the political economy. The extent of implementation and enforcement of the regulatory measures, as well as the degree of industry influence on the regulatory process, is also discussed.

Prior to 1961, government intervention in the industry was practically non-existent, and there had been no previous attempt to regulate the activities of the companies in the market. There had, however, been attempts to regulate the behaviour of motor vehicle owners and drivers by the passage of the Motor Vehicle (Third Party) Ordinances. This lack of control over company operations has been attributed to a number of factors, the most important of which appeared to be the domination of the market by foreign (mainly British) insurers (Falegan 1982(a),pp.189-190). Apparently it was not in their interests for any form of restriction or control to be imposed on the market at the time, since the lack of control measures in the insurance market enabled them to operate as they desired without any fear of intervention by the authorities.

The newly independent federal and regional governments of Nigeria appeared to take the view that government intervention in certain areas of activity were essential for the growth of the Nigerian economy. The First National Development Plan Document for the 1962-1968 planning period stated that "the Federal Government has an exclusive constitutional responsibility for certain major fields of governmental activity. These include...[among other things]...the creation of financial institutions appropriate to a sovereign state and the maintenance of confidence in these institutions."

The first piece of local legislation which was enacted to control the insurance industry was the Insurance Companies Act 1961.[1] The objective of this act was the registration of insurers by compelling them to register under the provisions of the Act. Since then, the government has employed various methods to control the insurance industry some of which have been the enactment of legislative instruments. Some of the legislation (The Insurance Companies Act 1961, The Insurance (Miscellaneous Provisions) Act 1964, The Insurance Companies Regulations 1968, The National Insurance Corporation Decree 1969, The Insurance Decree 1976, and The Nigeria Reinsurance Decree 1977) have been enacted specifically for the control of insurance company operations, while others (The Companies Decree 1968, The Indigenisation Decrees 1972-1977, among others) are of general application to the Nigerian economy as a whole. The legislative developments affecting insurers activities in the industry are summarised in Table 5.1.

5.1 The Objectives of Government Intervention in the Nigerian Insurance Industry

The objectives of government regulation of insurance business have been examined elsewhere.[2] In order to ascertain the objectives of government regulation of insurance business in Nigeria, two sources will be examined.

First, the objectives as stated by various public officials at different points in time are identified; and second, in the next section, the relevant legislative instruments will be examined in order to determine from their content the intent of regulation.

In Nigeria the main objectives of insurance regulation have been identified at various times as follows:

(1) To ensure that the operations and development of insurance are within the framework of the country's national economic and social objectives (Nwokolo 1984; Ojo 1986,pp.5-12).

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1. The Marine Insurance Act was also passed into law in 1961. This Act, however, was specifically "An Act to provide for marine insurance and to prohibit gambling on loss by maritime perils."

2. See chapter three.

Table 5.1
Developments in Insurance legislation in Nigeria 1960-1988

Legislation	Legislative Focus
Insurance Companies Act 1961	Policyholder protection
Insurance (Miscellaneous Provisions) Act 1964	Strengthen Domestic Economy
Insurance Companies Regulations 1968	Strengthen Domestic Economy and Insurance Market
Companies Decree 1968	Strengthen Domestic Economy
NICON Decree 1969	Strengthen Insurance and Reinsurance Market
Indigenisation Decrees 1972-1977	Strengthen Domestic Economy
Insurance Decree 1976	Policyholder Protection
Nigeria Reinsurance Corporation Decree 1977	Strengthen Insurance and Reinsurance Market
Insurance (Special Provisions) Decree 1988	Policyholder Protection
Privatisation and Commercialisation Decree 1988	Strengthen Domestic Economy and Insurance Market

(2) To conserve Nigeria's foreign exchange resources for developmental purposes[3] through the operations of the National Insurance Corporation of Nigeria and the Nigeria Reinsurance Corporation. In 1978, the Federal Commissioner for Trade[4] addressing an international reinsurance seminar stated that

> "...legislations establishing...national companies...[are] designed to improve insurance business...and give ...governments...the opportunity to participate in many aspects of insurance business...[and] national insurance companies...[are] meant to function as lead companies...to ensure that government policies are adhered to and also to assist in raising the standard of insurance companies operations...."[5]

He also stated that reinsurance institutions were established

> "...to ensure that the outflow of foreign exchange in the country is considerably reduced...[and to ensure] that the valuable financial resources were mobilised are essentially utilised for economic development purposes."[6]

(3) To ensure that the highest standard of discipline and integrity are maintained in the industry.[7]

(4) To ensure that insurance companies and intermediaries are lawfully established and conduct their business on sound insurance principles, so as to protect the interests of the insuring community,[8] and to prevent badly managed and undercapitalised companies from operating in the market, to support and protect

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3. See The First National Development Plan, that is, Federation of Nigeria, Federal Government Development Programme, 1962-1968, Sessional Paper No.1 of 1962,p.14, and see also Ojo, M.O., (1986).

4. The Ministry of Trade was the ministry which was charged with the control of insurance company operations at the time.

5. Statement made by Prof. I.U.W Osisiogu, see WAICA Journal, 1988, Vol.IV,p.12.

6. See also Statement by the Federal Commissioner for Trade, Major-General M. Shuwa, Journal Of The Insurance Institute of Nigeria, 1976/1977, Vol.V&VI,p.17.

7. Statement made by Ibrahim Babangida, the President of The Federal Republic of Nigeria in a presidential address on the occasion of the opening of "Reinsurance House". See The Risk Bearer, 1988 Vol.13(13), p.10. The Risk Bearer is the Journal of the Nigeria Reinsurance Corporation, a federal government owned company. Ibid,p.10

8. This statement was made by Eugene Okwor, the Director of insurance, Federal Ministry of Finance. See The Risk Bearer, ibid, pp.2-8.

the better run companies, in order to achieve an efficient and prompt insurance service.[9]

5.1.1 The Sources of Insurance Regulation in Nigeria

This section reviews the sources of regulation in the Nigerian insurance industry. Since the focus of this study is on the regulation of life insurance business, the review of the regulatory sources will be based primarily on their application to life business. Most of the provisions of the various legislative instruments examined, however, apply to both life and non-life business. The enumeration of these legislative instruments and the examination of their content is carried out in order to ascertain the change in regulatory philosophy over the time period under consideration, as well as the associated changes in regulatory objectives over time. It is appreciated that the enumeration of these regulations and their content is simply a statement of the intent or desire to regulate and does not throw light on what is actually being done, the impact of the regulations on the industry or the extent of enforcement of, or compliance with, regulatory measures.[10] Therefore these issues will be dealt with in the following sections[11] as well as in the next chapter.

5.2 Historical Background 1900-1959 (The Colonial Phase)

The insurance industry in Nigeria is known to have been in existence before 1900 (Okigbo 1981,p.154), more specifically since the late 19th century (Barback 1977). The industry was dominated by the early British merchants who had established trading posts on the west coast of Africa (Irukwu 1978,p.132). These merchants acted as agents for some British insurance companies and it is well documented that at least two British insurance companies appointed agents in Lagos, the capital of the country, to represent their interests well before 1900 (Okigbo 1981,p.154). The general agents so appointed were initially expatriate banks and trading companies although later on Nigerian traders and merchants were appointed (Adeyemo 1972,pp.90-91; Irukwu 1987,p.37). They had the power of attorney to underwrite and settle claims on behalf

9. Shuwa, ibid.

10. Stigler (1962,p.1) puts this across rather humorously "...if wishes were horses, one would buy stock in a harness factory", and El-Hassan (1981,p.ix) notes that "A legal doctrinal study preoccupied with the analysis of rules and procedures is unlikely to provide insight into how the institution operates...[and] is...unlikely to be of value when legal rules are not truly reflective of practice."

11. Sections 5.2.2 to 5.3.5.

of their expatriate principals (Ngwiri 1978,p.189). Through their activities insurance business became the virtual monopoly of British companies in the country (Olayide 1976,p.166). The general agents later appointed sub-agents and the resultant activity from their operations in the market eventually led to the establishment of some branch offices representing British insurers in Lagos, and subsequently, other principal towns.

The Royal Exchange Agency, the first insurance agency in West Africa, was introduced into Lagos in 1919 by the African and Eastern Trade Corporation (Braithwaite 1990,p.173). It later opened a full branch office in 1922 (Nwankwo 1980,p.115), having the distinction of being the first foreign insurer to open a branch office in Nigeria, and it remained until 1949 the only locally established company with an office in the country (Adeyemo 1972,p.92). Most of the other companies operated mainly on the traditional British agency basis mentioned above (Ojo 1976,p.48). The Royal Exchange initially concentrated on fire insurance business which was its main source of income and later branched out into general accident insurance business (Okigbo 1981,p.155).

At this time, the insurance market was not overly active, business consisting mainly of marine cargo insurance for produce exports, a few fire and burglary insurances of a personal nature, bank mortgage security, and a few motor insurances (McNesty 1973,p.37). Although there was at this time no active life insurance market, records do show that friendly societies existed from the late 19th century, and as at 1933 there were about 28 of them.[12] These were all established under the United Grand Lodge of England, Scotland and Ireland. They were instituted primarily for the object of freemasonry and, in the case of the Irish grand lodges, mutual aid. The number of members in individual lodges varied between 11 and over 400, the lodges being scattered over wide geographic areas-specifically Lagos, which had nine, Calabar, Warri, Port-Harcourt, Kano, Jos and Enugu. Only 6 kept invested funds, the amount of which varied from between £50 to £1,900.

In theory the activities in the market were controlled by the provisions of a UK statute, the Life Assurance Act of 1874, which was a statute of general applications as from the 1st of January 1900 (Nwokolo 1986,p.24). It is, however, doubtful whether the Act was indeed applied in practice and this has been attributed to the very small

12. Colony and Protectorate of Nigeria Blue book 1936, Federal Government Printer Lagos.

percentage of insurance business transacted in Nigeria at the time (Akinkugbe 1976,pp.57-8).

Several factors have been identified as having provided an impetus for the growth of general insurance business in the country at this time. First, the second world war which led to [some form of] social and technological progress; second, government legislation in the forties and early fifties which imposed such liabilities as Compulsory Motor Insurance and Workmen's Compensation on the public (McNesty 1973,pp.37-38); and third, the need to finance the marketing of produce since the banks always insisted on policies of insurance as security for advances (Falegan 1986,p.5). This led to increased activity in the Nigerian general insurance market.

Consequently, in 1945, three companies, The Norwich Union Fire Insurance Society (which now operates as part of The Guinea Insurance Company Ltd), The Tobacco Insurance Company Ltd, and The Legal and General Assurance Society Ltd commenced operations in the market (Okigbo 1981). There followed an influx of insurance companies which were subsidiaries of British offices. At this time there were no indigenous, that is, fully Nigerian owned insurance companies in existence (Okigbo 1981). This changed when Dr K.O Mbadiwe established the African Insurance Company, an indigenous company, in 1950 (Farnsworth 1975). The Nigerian General Insurance Company and The Lion of Africa Insurance Company, which was formed jointly with a British office, later came on the scene (Olayide 1976,p.166). The first crop of brokerage firms in the country were under foreign ownership,[13] and the first indigenous brokerage firm was owned by T.A Braithwaite, a Nigerian. This was followed by the establishment of 11 indigenous brokerage firms between 1959 and 1968 (Braithwaite 1990,pp.174-175).

Before 1960, life insurance was still not of any significant importance in the insurance market. There is not much statistical evidence available for the pre (and indeed much of the post) 1960's period but it is on record that life insurance business started much later than non-life business (Nwankwo 1980). In fact life business only started to attain some measure of importance in the 1960's (Ojo and Adewunmi 1982,p.162), nearly three quarters of a century after the inception of non-life operations in the market.

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13. C.T Bowring & Co.,1955, Glanvill Enthoven 1957.

The market was, relatively speaking, small. An examination of the list of registered insurance companies in various editions of the Nigerian Insurance Year Book shows that in the 1950's there were only three life insurance companies in the market: The Nigerian General Insurance Co., registered in 1951; The Lion of Africa, registered in 1952; and The Guinea Insurance Co., registered in 1958. These offices were all composites, underwriting both life and general insurance business. The African Alliance Insurance Company is said to have been the first specialist indigenous company to underwrite life insurance business only.[14]

Although the financial and legal barriers to market entry appeared to be low, the size of the market was small, both in terms of the numbers of companies underwriting this category of insurance, and the level of consumption of life insurance at the time. This could be attributed to a number of factors:

(1) The few companies in existence were not interested in insuring the lives of Africans mainly because of the alleged high costs of doing so.[15] This was a precedent set by the earlier (colonial) practitioners in the field who did not consider it worth while to assure the lives of Nigerians. The colonial view of African lives is illustrated by the following passage in a British history text on Nigeria:

> "The physique of the Negro is generally very fine, though there is often combined with a well-developed, muscular body an extremely feeble constitution which succumbs easily to disease...[b]oys and girls come to puberty at a very early age, and grow old more rapidly than does the European, the women particularly being passee at an age when an Englishwoman would be at the prime of life." (Burns 1972,p.62).

Consequently there was a "Tropical Loading"[16] imposed on premiums charged on Nigerian lives. This, coupled with the absence of adequate data from which realistic

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14. This statement is attributed to Chief M.O Odele, the then Managing Director of the Nigeria Reinsurance Corporation in The Sunday Vanguard, May 5 1991,p.15 and was confirmed by Mr. Ope Oredugba, the Chief Executive of The African Alliance during a discussion with him in July 1991.

15. Discrimination in respect of "negro" lives was a universal feature of insurance underwriting. See Kimball (1961,p.496).

16. The tropical loading was an additional expense factor computed into premium calculation to take into account the perceived additional risk involved in insuring such lives.

mortality tables could be computed, made both the purchase and underwriting of such policies unattractive to all concerned.

(2) Apart from this, socio-economic forces were involved. The industrial and commercial sectors of the economy were underdeveloped which meant that the levels of disposable income and savings was low. The existence of commercial banks and other forms of competitive savings media, such as the traditional financial institutions,[17] as well as religious attitudes predominantly among the Islamic population in the country, have been said to have negatively influenced the demand for life insurance (Ojo and Adewunmi 1982; Onoh 1980, pp.11-29).)

(3) Additionally, insurance services in general were not given priority in the national development plans implemented by the Federal Government. In the 1962-1968 plan, for example, in the proposed capital expenditure on trade and industry, insurance was allocated 2.3% of the total proposed expenditure, out of a total of 13.3% allocated to trade and industry, of which 9% went to the Nigerian Development Bank. The allocated expenditure was to be utilised solely for the establishment of an insurance company to take charge of the insurance of export crops.[18]

It can be inferred from the above that various factors contributed to the smallness in size of the life market. Apart from the issues raised the product offering was poor, whole life insurance being the only kind of product offering in the market. Almost all the life offices and their agents operated solely in Lagos so that the market was not geographically penetrated. Thus, not only was access to the product restricted to a certain geographic area, in addition the product-choice set was limited. All this coupled with an expensive product only served to severely restrict the demand for life insurance services, and since there were substitutes readily available the consumption of insurance services was at a minimal level.

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17. For example, the Isusu and Ajo traditional financial systems found among the Eastern Ibo and Western Yoruba tribes respectively.

18. See Federation of Nigeria, Federal Government Development Programme 1962-1968 Sessional Report No.1,pp.14-15.

5.3 The Post-Colonial Phase 1960-1988

5.3.1 The Era of The Civilians

As previously mentioned, before 1960 there was no specific local legislation governing the operations of insurance companies in Nigeria. This deficiency in legislation led to, among other things, a dearth in official statistics regarding insurance company operations, since they were not required by law to submit returns to the Insurance Division of the Ministry of Trade (Olayide 1976). In fact, for the period until 1967, the Federal Office of Statistics publications specifically stated that foreign insurers transacting insurance business in Nigeria were not required to submit data on their life insurance operations within the country (Ogunshola 1973,p.50).

5.3.1.1 The Insurance Companies Act 1961

The first attempt by the newly independent (civilian) government of Nigeria to control the activities of insurers operating in Nigeria was the enactment of the Insurance Companies Act, 1961. The Obande Commission Report (1960) formed the basis of this Act. The Commission had been set up by parliament to examine the question of the regulation of the insurance industry in Nigeria (Okwor 1984,p.33). The Act repealed the United Kingdom Life Assurance Companies Acts 1870,[19] 1871, and 1872 insofar as was applicable to Nigeria.[20]

The Act provided for the appointment of "a fit person" as the Registrar of Insurance as well as Assistant Registrars for the administration of the Act.[21] The Registrar of Insurance was under the Federal Minister charged with the responsibility for insurance.[22] The Act regulated three main categories of insurance business as follows: (1) licensing of insurers (2) solvency and business methods regulation and (3) amalgamations and, to a limited extent, investments.

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19. The main emphasis of this act was on policyholder protection as a result of many unscrupulous insurance companies that had been declared insolvent with a resulting loss to policyholders (UNCTAD TD/B/393, 1972,p.29).

20. Section 46.

21. Section 5.

22. Section (2).

No insurer could commence or carry out insurance business in the Federation unless such insurer was registered for the purpose of the Act[23] and, in the case of an external insurer,[24] the Registrar had to be satisfied that the insurer was duly registered under the laws of the country in which its head office was situated.[25] In addition the Registrar had to be satisfied that the business of insurance was or would be conducted in accordance with "sound insurance principles."[26] The paid up capital provisions discriminated between local[27] and external insurers, the capital requirements for the former being in the amount of not less than £25,000, and the latter not less than £50,000. If an application to underwrite insurance business was refused by the Registrar, the applicant could appeal to the Governor-General through the Registrar.[28] The Registrar could, under certain circumstances, cancel the registration of an insurer.[29]

No provisions were made in the Act for the licensing of insurance brokers and agents.

The Act imposed margin of solvency requirements for local and external insurers. For life insurance business the requirement was that the liabilities under unmatured life, industrial, and sinking fund policies should not exceed the amount of the local insurers life insurance fund.[30] For all other business it was required that the value of the assets of the local insurer in respect of the business which he underwrote should exceed the liabilities in respect of same by the amount of £25,000 (or its equivalent in another currency), or one-tenth of the premium income in the last preceding financial year whichever was the greater amount. In addition it was provided that for all classes of business, including life business, the value of the assets of the local insurer in respect of all underwritten business should exceed the amount of the life insurance fund together with all the insurers liabilities (excepting liabilities in respect of

23. Section 6(1).

24. An external insurer was defined as "an insurer carrying on business within or outside of the Federation whose head office is not in the Federation" (section 2), that is a foreign insurer.

25. Section 7(c).

26. Section 7(a).

27. Insurers whose head offices were within the Federation (section 2).

28. Section 8.

29. Section 9.

30. The life insurance fund was defined as the fund to which the receipts of an insurer in respect of his life insurance business are carried (section 2).

unmatured life, industrial insurance and sinking fund policies) by the amount of £25,000 (or its equivalent in any other currency) or one-tenth of the premium income (not being life insurance premium income) in the last preceding financial year, whichever is the greater amount.[31]

The requirements for external insurers and local insurers carrying on insurance business within and outside the Federation or solely outside the Federation were the same as for life insurance business[32] in respect of local insurers, but were more stringent in respect of non-life business (£50,000).[33] No provisions were made however as to the basis for determining the value of assets and liabilities. Although UNCTAD experts had recommended a "country-by-country"[34] approach to the valuation of assets as being the most appropriate way of determining the asset values by taking into consideration local conditions in each country, nevertheless they were of the view that such valuations should be made on a "prudent and conservative" basis to ensure the solvency of insurance concerns.[35] This requirement for prudence and conservatism was not addressed in the Act.

The Act also required an insurer to prepare and submit to the registrar within six months after the end of the financial year, a certificate of solvency signed by an actuary in the case of life business, a duly audited balance sheet, profit and loss account, a certified copy of the revenue account for life and non-life business, a statement of life insurance business which excluded industrial and sinking fund policies and other documents as required by the Registrar from time to time.[36] The accounts of local insurers were required to be audited annually by an auditor approved by the Registrar and the Act specified the duties of the auditor in this regard.[37]

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31. Section 4(1)(a).

32. Section 4(b)(i&ii).

33. Section 4(b)(ii&iii).

34. Such an approach would take into consideration local conditions in each country.

35. UNCTAD TD/B/393, 1972,p.13. "Insurance Legislation and Supervision in Developing Countries". Some of the problems involved in not establishing a specific valuation basis were identified by El-Hassan (1981) in his study of insurance regulation in the Sudan. They included wrongful and downright fraudulent valuations in order to give the appearance that the companies were solvent when in fact they were not.

36. Section 12.

37. Section 29.

The provisions in respect of external insurers in this regard were less stringent. They were merely required to keep a record of all local policies with the rights and obligations and premiums received thereunder as well as documentary evidence of their assets in the Federation.[38] With respect to the requirement for the annual audit, all the external insurer had to do was "furnish evidence to the satisfaction of the Registrar that its accounts are subject to an annual audit by an independent auditor."[39]

The insurer was required to maintain separate records for life insurance business, and the life fund was to be kept separate from receipts in respect of all other business in the interests of life policyholder protection. This requirement of separation of funds was not applicable to marine, aviation or transport insurance business.[40] The periodical investigation of long-term business[41] by an actuary at least once every five years was required. Amalgamations, transfers and acquisitions of long term business or workmens compensation business was not allowed unless the transaction was approved by the High Court.[42] With respect to investments, the regulatory requirements were concessionary and, not to say the least, ambiguous. The Act stated that

> "The Minister may if he thinks fit and not withstanding any other provision of this Act, require any insurance company to invest in Nigeria a percentage of the profits of the insurance company accruing in respect of its business in Nigeria, and not exceeding three percent in any financial year of the insurance company profits" (italics mine).[43]

Thus the Act concentrated mainly on specifying conditions for the registration of insurance companies in Nigeria, although a very slight tendency towards protectionism could be seen in some of its provisions.[44] A provision for the issuance of regulations was made in the Act.[45] However, although the paid-up capital requirements were heavier for external insurers, the provisions for the regulation of

38. Section 14.

39. Section 30.

40. Section 15.

41. Life, industrial and bond investment business (section 2).

42. Sections 17 and 18.

43. Section 28.

44. Sections 4 and 30.

their business methods was superficial and investment regulation was, to all intents and purposes, non-existent.[46] No provision was made in the act for the method to be used in the actuarial valuation of assets and liabilities for solvency purposes, which left the process subject to abuse.[47]

The provisions of the Act have been described as "scandalously inadequate". Apart from this the implementation and enforcement of its provisions was lax. In one case, the prosecution of an insurer who had contravened the provisions of the act with respect to registration requirements was not initiated until 5 years after the alleged offence had been committed. Even then the charge made was under the criminal code rather than under the Insurance Companies Act since "It never occurred to anybody to prosecute under the Insurance Companies Act" (Olawoyin 1976,p.63). In view of the laxity in regulatory control, it is not surprising that "...many insurers operate[d] on the fringe of the law, whilst others blatantly disregare[d] it" (Olawoyin 1976,p.62).

In addition some of the legislative provisions proved difficult to comply with. For example, although the Act required an actuarial valuation of long term insurance business once every five years, at that time, there were no professionally qualified Nigerian actuaries in the market (Adeyemo 1972,p.101).

In an attempt to stimulate the purchase of insurance products the government introduced a provision for life assurance premium relief. Section 17(5) in the fourth schedule of the Income Tax Management Act 1961[48] made provision for tax relief of not more than £1000,[49] in respect of individual insurances. Under the provisions of section 16(w) of the third schedule of the Act, the investment income of pension, provident or other "approved" schemes were exempted from taxation. This provision created discriminatory taxation with respect to insured pension schemes, because the pension funds of life companies writing pensions business were subject to taxation at

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45. Section 44.

46. It is only fair to note that the inadequacy of investment regulation applied to both local and foreign insurers.

47. Insurers could over-value assets and undervalue liabilities to comply with the solvency requirements.

48. This Act has been superseded by the Companies Income Tax Management Act 1979. The basic provisions with respect to insurance however remain unchanged.

49. The currency in use at the time was the Nigerian pound. The currency was later changed to the Naira in January 1973, and initially £1 was equivalent to ₦1.

the standard company tax rate, while the funds of the uninsured schemes were not taxed.

Another taxation problem arose with respect to the mode of taxation of life offices. The standard company tax rate, which varied from year to year, was applied to the investment income (less allowable expenses) of the life offices. An ordinary trading company could adjust the prices of the products it sold in line with the variation in company tax rates. However, life offices were not able to do this since the premium rates on life policies issued were usually fixed throughout the term of the policy (Ogunshola 1976/77,p.84).

5.3.1.2 The Insurance (Miscellaneous Provisions) Act 1964

In the 1960's, the dearth of indigenous capital and technical expertise in the economy had led the government to pursue industrial policies that encouraged direct foreign investment in the country.[50] At this time, most of the insurers in the industry were foreign. In 1960, during the debate on the 1960 Federal Budget, some politicians had demanded that the insurance industry be placed under public control. The Federal Minister of Finance, Chief Okotie-Eboh, responded to this demand in a manner that clearly stated the new governments stance on the matter;

> "This is a very serious matter. We all know that nationalization of industry is akin to communism (Several Hon. Members: No, no!). Yes, it is. This sounds all very simple but this simplicity is most misleading. First, this talk of nationalization is dangerous to our economy. All the Governments (of the Federation) have publicly declared that no steps of further nationalization beyond various public utilities will be undertaken. It is therefore shameful that the Leader of the Opposition (Chief Awolowo) who had been heading a Government and who is a party to this assurance comes here to call upon this Government to nationalize insurance which is a private enterprise (Shame, shame!). The new talk of further nationalisation can only frighten off those who wish to invest in Nigeria. Thus the first point is that his suggestion is economically dangerous. The second point is that insurance business is highly technical (Blunt 1977,p.81)."

It soon became apparent that many insurers especially the foreign insurers were not investing their funds in Nigeria.

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50. See section 4.1.1 of chapter 4.

The foreign insurers remitted most of their profits to their home offices so that capital was being extracted from Nigeria to the developed country capital markets such as the London market. Additionally, they were not investing their funds in Nigeria, at a time when the country was in need of capital for development projects.[51] This problem was however not specific to the life market, it affected the whole of the economy.[52] In response to this, the government passed the Exchange Control Act of 1962.[53] This act prohibited residents of Nigeria from making payments outside the country except with prior exchange control approval. However, the Act did not specify any penalty for its infringement and as such could not be effectively enforced,[54] and the flight of much needed capital overseas continued.

The situation appeared to be getting out of control and in 1964, the government took steps to keep capital in the country by enacting the Insurance (Miscellaneous Provisions) Act 1964. This Act established the office of the Inspector of Insurance who could also hold the office of the Registrar of Insurance.[55] Its main purpose was, however, to tighten the control over the investment behaviour of insurers in the market. It repealed sections 28 and 44(2)(b), the provisions relating to the investment of profits in the Insurance Companies Act 1961,[56] and required insurers to invest a minimum of 40% of their previous years premiums (less reinsurance premiums) and all endowment funds[57] in Nigerian investments.[58] Nigerian investments for the purpose of the Act were defined as government stocks, notes, bonds and other federal government securities, Nigerian company stock, shares and debentures, as well as the rights to receive interest or dividend on such securities.[59] There was a requirement for

51. Figures relating to the amount of funds remitted abroad by foreign insurers during this time are unavailable.

52. The effects of direct foreign ownership and control of some areas of economic activity in Nigeria are discussed in chapter four.

53. Under military rule, the provisions were tightened under the provisions of the Exchange Control (Anti-Sabotage) Decree 1977.

54. Alhaji A.O.O. Otiti, Executive Director (Operations), Central Bank of Nigeria. See WAICA Journal, 1978 Vol.1V,p.42.

55. Section 3. The powers of the Inspector of insurance have been described as "inquisitorial" (Nwokolo, 1986,p.11)

56. Section 7(4).

57. Section 2.

58. Section 2.

59. Section 5.

a minimum investment of 25% in government securities and a ceiling of 10% for investment in property.[60]

In addition to these measures, the Act made the provision that contracts of insurance in respect of local risks would be considered void unless the insurer was a Nigerian company.[61] However this was not a particularly stringent requirement as a Nigerian company was defined as "a company which is formed and registered under the Companies Act or which complies with the provisions of...that Act (which relate to companies incorporated outside Nigeria which establish places of business within Nigeria)..."[62] and so included foreign insurers. Again, as with the previous Act, any measures made as regards the domestication of insurance business were more apparent than real, since foreign insurers could still operate in the market without any serious restrictions on the establishment of foreign companies.

The 1964 provisions had been drafted by officials in the Ministry of Finance who had held meetings with the Nigerian Insurance Consultative Committee, who represented the insurance companies in the market. The Ministries of Trade and Justice were also involved in drafting the Act. When the Act was being considered by parliament in 1964, some members again raised the issue of the nationalisation of the insurance industry. Chief Okotie-Eboh's response to this was;

> "I must say...that we do not contemplate in this country, the nationalisation of insurance business...Nationalisation is not our policy...It is not the policy of this Government to nationalise any private industry. When the time comes for us to set up our insurance business, we will do so" (Proehl in Akinsanya 1983,p.156).

This was the first intimation that the government was planning to establish a national insurance company.

The provisions of the 1961 and 1964 acts could, however, not be implemented due to enforcement problems, and there were deficiencies in the regulations.[63] Both acts were in fact not gazetted until years later, on the 11th of May 1967. They were however retroactively brought into force from the 4th of May 1967.[64] The acts were

60. Section 5(2).

61. Section 1(1).

62. Section 6.

patterned after British enactments which were aimed at ensuring "freedom with publicity" and solvency to the industry as opposed to a close system of control and supervision.[65] The powers of the Registrar of insurance under the Act were limited and many potential new entrants into the industry devised a way of obtaining the capital licensing requirements by arranging with commercial banks who would initially make the deposit available to satisfy the legal requirement and afterwards withdraw the deposit (Okigbo 1981,p.157). Although it was the general feeling at the time that the two acts should be co-ordinated and enforced, difficulties arose with respect to their implementation and this resulted in delays. The government did not possess officials with expertise in this area and as such it had to resort to requesting for assistance from a foreign organisation (Okwor 1984,p.34; Falegan 1991,p.242).

The request for assistance was made to the United Nations Technical Board which was requested to formulate proposals for merging the two acts and rectifying their defects. The Board responded by providing the government with the expert assistance of Dr. Karl Reichel, an UNCTAB expert. Subsequently, in 1966, Dr Reichel was appointed the Federal Government Adviser on Insurance Matters. His assignment was to formulate policies on insurance matters and to assist in the establishment of a national insurance company (Okwor 1984,p.33). Under his leadership it was recommended that the Insurance Acts of 1961 and 1964 be repealed and replaced by a new and comprehensive act.

Reichel started work on drafting a new insurance bill and accompanying regulations, and by the end of 1967 he had completed the draft bill. The bill contained stricter control measures for the regulation of the industry because Dr. Reichel was of the opinion that "such a system was more appropriate for developing countries where insurance has to be guided to a certain extent, often from its infancy, to a sound stage of development" (Falegan 1991,p.254). The provisions of the draft bill had been extensively discussed and commented upon by officials in the Ministries of Trade, Justice, Finance, Industries, Labour, and Economic Development. The Federal Executive Council, as well as the Foreign Legislation Division of Lloyd's, were also involved in the process. The insurance industry, represented by the Nigerian

63. Reichel 1966-71 in Falegan 1991.

64. Journal of The Chartered Insurance Institute, Vol.65 1968,pp.312-313.

65. Insurance legislation in the developing countries is sourced from either the UK enactments or the legislation of the European countries, especially France. It has been observed that the UK which developed the "freedom with publicity principle" is gradually moving towards tighter regulation. See UNCTAD TD/B/393, 1972,pp.30-32 and also more recently the UK Financial Services Act 1986.

Insurance Consultative Committee,[66] is reported to have received the bill well because "Its objectives were to safeguard the interests of the insuring public as well as the insurance companies themselves" (Falegan 1991,p256). The bill was to be called "The Insurance Supervision Decree of 1967."

This period was one of serious political unrest in the country. The political situation was tense and extremely volatile,[67] and the military decided to intervene. In July 1967 the military took over from the democratically elected civilian government,[68] and it was unclear what effect this change of governance would have on the decision making processes of government with respect to legislative decisions.

Under civilian rule, draft bills of proposed legislation in the area of insurance activity had been the subject of intense discussion and analysis by both industry and government officials and foreign expert advisers.[69] Under colonial rule and indeed for some years afterward, Nigerians had been subjected to oppression and had been marginalised in the public and private sectors (Ogunlana 1985,p.33). Very few had been encouraged to acquire expertise in key areas of the economy.[70] Thus, in drafting and passing much of the legislation in force at this time, the assistance of various experts was employed, and quite naturally, industry advice would have been taken into consideration in the passage of these Acts. It is therefore not surprising that the 1961 and 1964 Acts were patterned after the British enactments since the dominant insurers in the market at the time were British. The prospect of continuing to dominate the insurance market (as well as other sectors of the economy) must have been very appealing to the former colonial rulers. Nigeria was Britain's largest market in Commonwealth Africa[71] and the British were concerned to maintain the status quo.

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66. The Nigerian Insurance Consultative Committee represented 46 of the 92 registered insurance companies in the market at the time (Falegan 1991,p.256).

67. This is discussed in chapter 4.

68. See chapter 4, section 4.2.2.

69. For details see Falegan (1991,pp.241-278).

70. The colonial extreme prejudice towards "Negroes" formed the basis of the neglect of Nigerians in the country. This prejudice extended far back into the 16th century, when the west coast of Africa was being explored. Burns (1972,p.63), quotes a traveller who wrote that the "Negroes [are] a people of beastly living, without a God, laws, religion or commonwealth", and another who said they "are all without exception Crafty, Villainous, and Fraudulent, and very seldom to be trusted; being sure to slip no opportunity of cheating a European...[a] man of integrity is as rare among them as a white falcon...and it would be very surprising if upon a scrutiny into their [l]ives we should find any of them whose perverse Nature would not break out sometimes; for they seem to be born and bred villains."

Thus it is perhaps understandable, if not justifiable, that the British insurers did not encourage extensive Government participation in the insurance market. These insurers were accustomed to operating under relatively liberal market control rules with their emphasis on "freedom with publicity."[72] This provided a situation in which insurance companies were given a lot of latitude with respect to their operations. Their detailed operations in the area of, for example, investments were not monitored. The supervisory authority was mainly concerned with ensuring that the insurance companies remained solvent, and independent actuaries and auditors in individual companies were charged with the responsibility of determining insurers solvency. The supervisory body concentrated primarily on the local operations of these companies.[73] Thus like the case with many other developing countries[74] the British enactments and supervisory model were applied to the Nigerian insurance market, to the benefit of the foreign insurers. The socio-economic situation of the country was not taken into consideration. The lack of managerial expertise among indigenous insurers was intentionally or unintentionally overlooked. Many of the indigenous insurers operating in the market at this time were undercapitalised and lacked adequate skilled personnel. The laxity in regulation and supervision enabled them to continue operating and the insuring public in many instances fell prey to companies which were unable or unwilling to pay compensation. The foreign insurers did not suffer from these constraints and were able to make huge underwriting and investment profits from their business in the country.

The new military government were well acquainted with the general laxity in the regulation and supervision of the economic activities of the country. In colonial times, regulatory control over economic activity was firmly in the power of the British and Nigerians had no say in the matter. Although after independence in 1960, it appeared that the power to control economic activity in the area of insurance had been handed over to the Nigerians, in reality, this was not the case. Foreign vested [European] interests were still in control of economic activity in the country, while the Nigerians who badly needed foreign assistance, both financial and managerial, became unintentional or possibly more appropriately, ignorant pawns in this political farce.

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71. See Lloyd's Bank Ltd Overseas Department-Export Promotion, Economic Report on Nigeria, various issues.

72. See, for example, Supple 1984 and Westall 1990 for the history and regulation of insurance in Britain.

73. See UNCTAD TD/B/393, op.cit. p.33.

74. UNCTAD TD/B/393, ibid.

5.3.2 Under Military Rule

5.3.2.1 The Insurance Companies Regulations 1968; The Companies Decree 1968

The mass proliferation of insurance companies in the market without accompanying supervision was not in the public interest and, as such, the Government attempted to impose some form of control by enacting the Insurance Companies Regulations in 1968 (Okigbo 1981,pp.157-158; Falegan 1991).

Although discussions pertaining to the passage of the regulations had been going on during the civilian era, it was not until the 10th October 1969, that the regulations were gazetted. They came into effect retroactively from the 4th May 1967, when the 1961 act was brought into force.[75] The regulations made it compulsory for all foreign insurers in Nigeria to incorporate locally in order to be able to register as insurers in the country. Thus the foreign insurers operating in the market through the activities of their branches were by law precluded from doing so. The tone of the regulations was an indication of the future stance of the military government as regards the role of foreign investors in Nigeria. However at this time the military had a war to fight and win[76] and most of their energies and resources were devoted to doing just that. It appeared that the military rulers laid down the general tone for regulatory action and left the civil servants to the mundane business of debating and drafting legislation while they went off to fight.

The effects of the continuing foreign dominance of economic activity in the country was, however still, an issue which the military was concerned about, and a shift of policy towards foreign investment appeared to be in the making. In 1968, the Companies Decree 1968 was, in military parlance, promulgated. It was gazetted on the 16th October 1968 and brought into force retroactively from the 1st October of the same year. The speed with which the Decree was gazetted appeared to be an indication of the importance of the subject matter of the decree to the military authorities. Like the previous[77] legislation, it was patterned largely on the UK Companies Act 1948. However it decreed that all foreign companies operating in the country were as from the 18th of November 1968 to be considered as separate entities from their parent companies in respect of their operations in Nigeria. The companies

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75. Journal of The Chartered Insurance Institute, Vol.66 1969,p.254.

76. The Nigerian civil war, 1967-1970 (see chapter 4, section 4.21).

were required to inform the Registrar of insurance within a three month period from the 18 November of their intention to either continue operations in Nigeria or to withdraw from the country.[78]

It is on record that the insurance companies for the most part completely disregarded these requirements.[79] As stated earlier the military were busy defending the sovereignty of Nigeria and presumably did not have either the time, or the inclination, to supervise compliance. The fact of the matter was that the department charged with the supervision of insurance company activities, like so many other civil service departments at the time, was ill-equipped (in terms of both the quality of expertise and the amount of manpower required) to do so. It was not until July 1970, after the war had been fought and won, that the Government got around to gazetting the list of insurance companies authorised to transact business in the country.[80]

Meanwhile, the work which had earlier begun on the draft insurance bill, ran into some problems. One of the problems was that portions of the draft bill conflicted with the Government's policy towards foreign participation in the Nigerian economy. The relevant sections of the Companies Decree imposed the requirement that all such companies should incorporate locally or, alternatively, withdraw from the country. On the other hand the draft bill permitted the operation of foreign insurers in the country. Although Dr. Reichel attempted to convince the Government that this provision did not in any way conflict with Government policy, he was not successful. In addition to this the Government was preoccupied with matters of war. Discussions on the bill therefore stopped and it was in effect killed.

5.3.2.2 The National Insurance Corporation of Nigeria (NICON) Decree 1969

The Civilian Government's encouragement of foreign investments in the manufacturing and service sectors had led to the establishment of a viable manufacturing sector and this, coupled with other factors, led to the rapid economic growth experienced in Nigeria during the 1960's. This development was however

77. The 1961 and 1964 Acts.

78. See section 8 of the Companies Decree 1968 and The Journal of The Chartered Insurance Institute, Vol. 66 1969,p.254.

79. See Reichel (1966-1971), "Report on Insurance in Nigeria", Lagos: Federal Ministry of Trade, in Falegan op.cit at page 273.

interrupted by the adverse effects of the civil war. The ravages of the war caused the ruling military government to implement policies of reconstruction and rehabilitation.[81]

One of the ways in which the reconstruction and rehabilitation of the economy was tackled was by the implementation of policy measures aimed toward the domestication of the manufacturing and services sectors of the economy. Provision had been made in the First National Development Plan for an insurance company to handle the insurance of crops. The purpose for the establishment of the company was to conserve the country's foreign exchange resources for national developmental purposes.[82] This company, at the time, had not yet been established. Based on information available from a number of reports, the Government had decided to limit the scope of the proposed company to certain classes of insurance business. Advice from "local experts" in the insurance market, however, seemed to indicate the unworkability of the proposed national insurance company. They advocated the establishment of a national reinsurance company in addition to a national marine insurance company. Feasibility studies carried out by foreign insurers, however, indicated that this course of action was uneconomical.[83]

Meanwhile there appeared to be growing dissatisfaction in some Government and industry circles as to the performance of some of the insurance brokers and agents in the market. There were allegations that the brokers inflated sums assured in order to receive huge commissions, and that they did not remit premiums received from policyholders to the insurance companies for periods of up to two years. It was additionally claimed that some brokers received premiums for risks which they did not insure. Unethical practices occurred. Some top officials of Government bodies and corporations were said to have been appointed directors of the insurance companies with which they placed their insurances (Adebowale 1979,p.53). Insurance agents were said to be unskilled and inadequately trained (Aigbe 1982,p.8), misrepresented facts in order to make a quick sale (Kiladejo 1987,p.103), and were perceived by the public as school drop-outs who had nothing going for them. The agents were easily identified by their old briefcases, narrow ties, weatherworn jackets

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80. Reichel (1966-1971), ibid.

81. See chapter 4, section 4.2.1.

82. See Federation of Nigeria, Federal Government Development Programme 1962-1968, Sessional Report No.1 of 1962,p.4.

83. See Reichel (1966-1971) op.cit at page 243.

and more often than not, dusty shoes (Ogunrinde 1983, Uzoma 1978,p.11). The Director of Insurance, remarking upon the activities of insurance agents during this time, described them as uncontrolled, unsupervised and unorganised (Okwor 1094,p.35), and the industry was referred to as having been "...inundated and...infested by not too qualified and...illiterate canvassers.[84]

In response to the situation in the market, on 1 July 1969, the Military Government promulgated the National Insurance Corporation of Nigeria Decree which provided for the establishment of one national insurance company, The National Insurance Corporation of Nigeria (NICON) a national insurance company with an initial share capital of £1000,000.[85] The purpose for establishing this company was not, however, for the insurance of crops. Its objective were:

(1) To compel all insurers in the market to reinsure with the corporation at least 10% of the premium on every policy issued or renewed by them on or after the 1st October 1969.[86] The purpose of this was to promote reinsurance in the industry and reduce the outward flow of funds due to reinsurance outside the country (Ojo 1986,p.5).

(2) Additionally, NICON was to insure any property of the State or Federal government, or statutory corporation in which they had an interest. NICON was also to operate in the capacity of an insurance agent or broker in relation to the insurance of the aforementionned property,[87] and was given the discretion to either refuse or accept such reinsurances. NICON also had the power to determine the amount of commission payable on such business.[88]

(3) NICON was also established to assist in manpower development in the industry (Ojo 1986,p.5).

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84. See address given by the Lagos State Commissioner for Education to the Nigeria Insurance Institute, in Conference Papers of The Insurance Institute of Nigeria, Vols. V &VI 1976/77,p.22.

85. Section 11(1).

86. Section 8 (1).

87. Section 4(2).

88. Section 8(2)

However, life, fire and marine insurance business were exempted from the provisions of section 8 by the Exemption of Certain Classes of Insurance Business Order 1969.[89]

The NICON decree was not well received by various interest groups within the industry. By the provisions of the decree, NICON was enabled to act in the capacity of both an underwriter and broker with respect to all Government property insurances. This meant that all the non-life insurance companies in the market were precluded from a huge portion of insurance business, the insurances of government property. In addition, section 5(2) granted the corporation discriminatory tax concessions by providing that it would not be liable to taxation "until the amount in the general reserve fund of the Corporation is for the first time equal to the amount of paid-up capital of the corporation." This provision was applicable to NICON only and did not extend to other companies in the market. The insurance market viewed the establishment of NICON as a sly attempt to nationalize the insurance industry. As a leading broker (Braithwaite 1990,p.176) in the market put it,

> "The effect of the creation of NICON on Nigerian brokers was devastating...with one stroke of the pen, the livelihood of indigenous insurance brokers came to a stop; because at that time, up to 1969, most of the indigenous insurance brokers concentrated on the business of the Federal Government parastatals..."

Braithwaite was unimpressed with Dr. Reichel who had been instrumental in the drafting of the decree.

He was referred to as a "so called expert...who did not appear to know much about international business and was not prepared to accept help from anyone". It is apparent from the comments that some groups in the industry felt that they had not been consulted in the process leading up to the promulgation of the decree (Braithwaite 1990).

The Government through the operations of NICON was in effect operating as a regulator, an insurance company, an insurance broker as well as majority shareholder in the area of insurance and reinsurance in the economy. Many regarded these roles as conflicting (Ogunlana 1972; Okediji 1986(b)) and others were concerned that NICON did not have the managerial expertise to perform the brokerage function. Instances are given of times when the government, having spent a great deal of money (in one case about £11,000)[90] were unable to negotiate and collect compensation for some aviation

89. Journal of The Chartered Insurance Institute, Vol.67, 1970,p.269.

and marine losses because NICON lacked skilled brokers. The corporation in many cases had to resort to the services of one the leading private brokers in the market in order to negotiate and collect compensation from their overseas reinsurers (Braithwaite 1990,pp.175-181).

The managing director of NICON defended the company's position by stating that NICON's role in the industry was justified because of the existence of [unspecified] market imperfections. His view, which in effect was the official government line, was that NICON had to play these multiple roles in order to remove the foreign domination of insurance business in the country (Lijadu 1987). The official line taken by the government in response to criticisms of its action with regard to NICON was that

> "...no attempt has been made by government to restrict the operations of the privately owned companies and there is no nationalisation of the industry. Private companies operate in free and open competition with state-owned insurance companies."[91]

However it appeared NICON was unable to effectively discharge its brokerage functions both locally and overseas. Premiums were not remitted to overseas underwriters promptly, with the result that many claims were unpaid by these underwriters. Eventually some of its customers applied to the government to allow them to appoint their own brokers, and in 1976 the Government granted their request. This was "...the beginning of the end of the insurance broking function of NICON", and soon the indigenous brokers were back in business (Braithwaite 1990,p.182).

5.3.2.3 The Indigenisation Decrees 1972-1977

Although the quantum of legislation affecting insurance company activities had increased since 1960, the regulations were still seriously lacking in content. All classes of insurance business were still, in effect, accessible to foreign insurers and there were no restrictions on the classes of insurance business that could be purchased directly from abroad. Additionally, the Government did not regulate tariffs in any

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90. In this specific case the money was spent on airline tickets and hotel fees for two officials who were sent to London to negotiate and collect an aviation claim. When they did not succeed in doing so, two government delegations were despatched to London to resolve the matter. They also failed (Braithwaite 1990, pp.175-181).

91. The Risk Bearer 1988,p.4.

class of business, as a consequence of which premium rates were high (Adeyemo, 1972,p.101). None of the acts specified minimum requirements for the establishment of mathematical reserves, unexpired risk reserves, and the reserves for outstanding claims, as well as their valuation basis. There were also no rules regarding the evaluation of investments and apart from margin of solvency and capital requirements, no other financial guarantees were required in respect of insurers operations. Although the regulations appeared to provide for the localisation of insurance business by requiring foreign insurers to incorporate locally, this was a superficial measure since there were no criteria to determine the ownership structure of these companies. Thus, although for the purposes of the law a company could be classified as a Nigerian company, it could actually still be owned 100% by foreigners.

The resultant effect of this was that the insurance industry was still at this time dominated by foreign insurers and many incapable and fraudulent entrepreneurs were taking advantage of the lack of effective supervision to form financially unstable companies (Okwor 1978).

The problem of the dominance of foreign capital was not limited, however, to the insurance industry alone. In many sectors of the economy, foreign capital had gradually taken over.[92] In order to tackle this problem during the second development plan period, the military government in power promulgated the Nigerian Enterprises Promotion Decree 1972.[93] This was the first indigenisation decree which was aimed at increasing the participation of Nigerians in all the economic activities in the country. It was however silent on some business activities such as insurance which meant that foreigners could still have exclusive ownership and control of insurance business in the country.

Subsequent amendments and updates of the decree resulted in the final legislative instrument, the Nigerian Enterprises Promotion Decree 1977,[94] under which all businesses were classified into three schedules. As with the earlier decree, schedule 1 enterprises were the exclusive preserve of Nigerians, while schedule 11 contained a list of 57 enterprises in which the equity participation of Nigerians could not fall below a minimum of 60%. This schedule included life insurance business. In addition

92. See chapter 4.

93. The decree is discussed in chapter 4 section 4.

94. See chapter 4, section 4.

to this indigenisation measure, the Federal Military Government acquired 49% of the equity of all foreign insurance companies in the country.

5.3.2.4 The Insurance Decree 1976

Despite the passage and implementation of the enterprises promotion decree, distortions were still apparent in the market. The transfer of shareholdings from foreign to local participation was a slow and laborious process and many dishonest insurers who had no intention of compensating their policyholders in the event of a genuine claim were operating in the market. Others were financially unsound and could not, even if they had wanted to, satisfy the claims of their policyholders. Producer interests were effectively being served rather than consumer interests. The continuing foreign domination of the market by foreign insurers was apparently not in the national economic interest. Additionally the activities of insurance brokers and agents were not subject to any form of legal supervision. Insurance contract terms and other policy documents were not supervised, so that policyholders were invariably prejudiced in cases of disputes between insurance companies and insureds. The policy terms of most insurance contracts at this time were described as "unfair" and "oppressive", with policy terms being "treacherous". Some of the companies indulged in "sharp practices" (Osinubi 1990). To make matters worse, the courts sometimes enforced some of these terms enabling "...insurers to defeat the...honest claims...on mere legal technicalities" (Anifalaje 1984,pp.84-7).

The Government was aware of the problems in the insurance market. In the Third Development Plan Document it stated that

> One of the main problems in the insurance subsector is the multiplicity of insurance companies-both underwriting and broker [and]...the tremendous foreign exchange leakage caused by (a) the re-insuring of a large percentage of the risk outside the economy and (b) the dominance of foreign companies in the sector."[95]

In the Plan, Government had also listed as its policy main policy objective the elimination or mitigation of many problems in the economy, including those specified for the insurance sector. One of its objectives in this regard was to "narrow the zone of official ignorance in the Commerce and Finance sector and increase contact with the economic agents in the private sector."[96] This implied a willingness on the part of

95. Federal Government of Nigeria Third National Development Plan, 1975-1980 Vol.I at p.184.

the Government to listen to suggestions or recommendations by insurers as to the way in which the problems in the insurance market could be dealt with legislatively.

Meanwhile Nigeria's fortunes had changed. In 1969, oil had been discovered in the south western part of the country and the country was beginning to "enjoy" the benefits associated with this. The liquidity in the economy increased and many entrepreneurs decided to enter the insurance sector of the economy, thus compounding the problems in the already inefficient regulatory control system.

Pressure was continuously exerted by consumers and some insurers on the Government to actually do something about the situation. The older more established insurance companies were pressurising the government to flush out what they referred to as "mushroom"[97] insurance companies. Some insurers called for the government to increase the paid-up capital requirements which were considered as inadequate by some of the bigger, older more established insurers in the market (Ogunlana 1972,p.99). Ostensibly the reason for this was to rid the market of inefficient, undercapitalized and possibly fraudulent companies. However, others[98] in the industry felt that the bigger companies simply wanted to maintain the status quo by encouraging and entrenching their exercise of monopoly power in the industry. It was suggested that what the industry needed was not more regulation (except in the area of raising the entry requirements), but self regulation (McNesty 1973,p.41).

Meanwhile, a change of leadership occurred in the military. General Yakubu Gowon, the incumbent head of state was deposed in what was referred to as a "bloodless" military coup d'etat in July 1975. General Murtala Mohammed's style of governance was very radical, and the effects were felt in the insurance market. At this time, the Government started to implement its policy of increasing its contacts with the various subsectors of the economy. It commenced negotiations with the Nigeria Insurance Association with the specific objective of reducing motor insurance premium rates. This was its first attempt at the control of non-life insurance rates. However, despite industry reservations as to the ability of the insurers to operate effectively under a system in which motor premiums were subject to control, the rates were reduced. This

96. Ibid.,p.185.

97. The relatively smaller (in terms of premium income and size of labour force) and undercapitalised companies in the insurance market.

98. See for example, the Business Times, Monday June 2 1986,p.7.

proved to be the genesis of a somewhat stricter control of insurance market operations (Ogunshola 1976,p.65).

In 1976, under the Obasanjo regime, the Federal Government promulgated a new decree, the Insurance Decree 1976 which came into effect on the 7th December 1976. The Insurance Regulations of 1977 were issued pursuant to the decree.[99] The 1976 decree repealed the Insurance Companies Act 1961 and the Insurance (Miscellaneous Provisions) Act 1964. Some of the provisions of these Acts were re-enacted while some new provisions were made.[100]

Provision was made for the establishment of the post of the Director of Insurance and the decree became the main legislation governing the operation of insurance business in Nigeria. It dealt to varying extents with financial, product and business methods regulation of insurance business in Nigeria, and classified insurance business along two main categories, life and non-life insurance. Non-life business was further classified into fire, accident, motor vehicle, workmen's compensation, and marine, aviation and transport insurance business.[101]

The Director of Insurance stated that the objective of the decree was "...to ensure the effective control and supervision of the activities of insurance companies" (Okwor 1984,p.34). The explanatory note to the decree states that apart from this some of the other provisions contained in the decree "...relate generally to the better management and regulation of insurance business in Nigeria."

Section 8 detailed the licensing requirements for carrying out insurance business. These requirements were more stringent than the provisions contained in previous enactments. The Registrar had to be satisfied that among other things the class of insurance business for which an application was being made would be conducted in accordance with "sound insurance principles", and that "adequate and valid" reinsurance treaties in respect of every class of business were arranged. In addition the registrar had to be satisfied that the proposal forms, terms and conditions of policies were "in order and acceptable" and that there was at least one "competent and

99. Schedule 2 of the 1977 regulations relating to the prescription of registration fees payable by insurance intermediaries was subsequently amended by the Insurance (Amendment) Regulation 1983. The various fees were increased.

100. See the "Explanatory Note" to the 1976 Insurance Decree.

101. Section 2.

professionally qualified" person to be placed in charge of each department of insurance business.[102] The conditions under which the registration of an insurer could be cancelled were also set out in sections 7(a)-(r) of the decree. The paid-up capital requirements were ₦500,000 for an applicant for life insurance business and ₦300,00 in respect of non-life insurance business. For reinsurance business the requirement was for at least ten times the preceding amounts.[103] In addition to this every prospective applicant was required to deposit such share capital with the Central Bank of Nigeria for the period of time during which the insurer was engaged in the transaction of insurance business in the country. The Director of Insurance was permitted to release not more than 50% of this statutory deposit to the insurer after registration had been completed.[104] The Director could also release, if the insurer so required, not more than 25% of the statutory deposit in a situation where the insurer had suffered a substantial loss that could not be reasonably met from its own resources. This however had to be replaced within thirty days after the withdrawal date.[105]

The decree introduced more domestication policies by increasing the percentage of assets required to be invested in Nigeria to 100% for all classes of business and, in addition to specifying the categories of permissible investments, stipulated that not more than 10% of the non-life fund, and 25% of the life fund respectively could be invested in real property.[106] Provision was also made for the establishment of various reserves in respect of life and non-life business,[107] although as with the previous enactments, no bases for the valuation of assets was stipulated.

Rate regulation was also included in the decree. No insurer or group of insurers in the form of an association was allowed to make rate increases without the prior approval of the Director of Insurance, and the decree made provision for the Commissioner of Insurance to appoint "from time to time" a rating committee to review rates. The rating committee was to consist of industry representatives and their functions among other things were "to ensure that rates are non-discriminatory...to

102. Section 5.

103. Section 8.

104. Section 9.

105. Section 10.

106. Section 18.

107. Section 17.

examine...applications for general increase in rates and premiums...having regard to general anti-inflationary measures...and to review insurance commissions from time to time."[108]

Section 19 provided for the regulation of the accounts of the insurer and made specific provisions for life insurers to submit an abstract of an actuary report and a valuation report, a summary and valuation of life policies, as well as information as to premiums, policy reserve values and guaranteed surrender values, among other things. Non compliance with these provisions made the insurer guilty of an offence and liable on conviction to a fine of ₦2000. Section 20 made it mandatory for the insurers accounts to be audited annually.

The decree incorporated product regulation by requiring the prior approval of all insurance policies, documents and certificates of insurance, as well as any changes to be made to these documents.[109]

For the first time in the history of insurance regulation in the country, the regulation of intermediaries was incorporated into the provisions of the decree. Section 25 made it mandatory for insurance agents to be licensed under the provisions of the decree, while section 26 stipulated that premiums collected by agents should be remitted to the insurer within a maximum period of 15 days. Section 27 dealt with the licensing of insurance brokers. Brokers were subject to more stringent requirements. They were required to, among other things, deposit the sum of ₦25,000 with the Central Bank, to maintain a minimum professional indemnity insurance cover of ₦50,000 or 25% of annual brokerage fees in the preceding year, whichever was the greater amount, and were subject to higher penalties than applicable to insurance agents for infringement of their duties under the law.[110] The decree prohibited the rebating of commissions and premiums (except as prescribed).[111]

The 1976 decree was a comprehensive piece of legislation. It increased the scope of regulation by making provision for the regulation of the financial, product and business methods aspects of insurers. It appeared to raise the barriers to entry into the

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108. Section 33.

109. Section 14.

110. See sections 26(3) and 28(3) & (4).

111. See section 47.

industry by increasing the capital requirements in respect of all classes of insurance business considerably (from ₦50,000 (£25,000) to ₦500,000 in the case of life business). Apart from this, it also appeared to place restrictions on the category of people who could establish insurance companies by requiring that "there is at least one competent and professionally qualified person to man each department of insurance business."[112]

The regulation of rates in non-life insurance business[113] was introduced, and although life insurance rates were not directly regulated by the act, the provisions for the control of the investment behaviour of insurers was an indirect way of controlling life rates.[114] Although the decree specified maximum rates of commission in respect of non-life business,[115] it was silent on commissions in life business. The decree required life companies to establish a general reserve fund and a contingency reserve in respect of life business. The requirement is that the general reserve will be maintained with an amount which is equal to the net liabilities on policies in force at the time of the actuarial valuation.

The contingency reserves should be at least 1% of premiums or 10% of profits whichever amount was greater, with the reserve accumulating until it reached the amount of minimum paid-up capital.[116] The method for determining the solvency of the life fund was left to the discretion of the actuary handling individual company returns, so that different insurers in the market use different methods of computing solvency.[117] Since the basis for determining the value of insurer assets and liabilities was also not stipulated by law, this constituted a potential area of abuse by insurance companies, since incompetent insurers could conceivably falsify the figures to maintain a semblance of solvency.

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112. See section 5(1(f)).

113. This came in the form of prior rate approval. While tariffs exist for workmens compensation and motor insurance business, other types of non-life policies have minimum rates of premium specified. However, applications for rate increases had to be processed by the insurance department.

114. This is because in life business, premium rates are calculated upon a consideration of interest rates on the life insurers business, the expenses of management as well as the future mortality experience of the life portfolio.

115. See section 34(1(a&b)).

116. See section 17(3(a&b)).

117. Information obtained from the Insurance Department, Federal Ministry of Finance, Lagos in May 1991.

From the provisions of the decree it is apparent that the main focus was on policyholder protection, that is, the protection of the public interest. There was no need to address the issues of domestication of business in the decree because the Government had implemented this by use of other legislative provisions applicable to the economy as a whole and the insurance market in particular.[118]

Various sectors of the market had different views on the new decree. The Government saw it as the means to consolidate the market and ensure that insurance business was run along actuarially sound basis in the interests of the policyholder, and the comprehensiveness of the decree led to it's being described as "...an excellent document to serve as a legal basic protection of the public..." (Graves 1976,p.166). The Government also declared that the decree had "revolutionalised the industry and resulted in its efficient" regulation in accordance with the provisions of the decree.[119] It was also stated by the Director of Insurance that "The two principal objectives of the decree was to ensure, as a means of control, that insurance companies, brokers/adjusters and agents are lawfully established and operated at all times on sound insurance principles, and also to give better protection to members of the public."[120]

However, it was also considered that the decree had several "objectionable features" especially with regard to entry requirements, the investment of insurance funds, and the extensive powers accorded to the Director of Insurance. With regard to the capital entry requirements especially, it was stated that the new law was

> "prohibitive and...promoted by men...motivated by self-interest...it has restricted competition and protected entrenched positions...enshrined a likely monopoly by the present successful insurers"(Falegan 1982(c)).

Falegan went on to state that the powers granted to the supervisory authorities under the decree were too wide and dictatorial despite the fact that the Nigerian experience had

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118. The Companies Decree 1968, NICON Decree 1969 and Indigenisation Decree 1977, among others.

119. The Risk Bearer 1988,p.3.

120. Okwor 1984,p.34.

"demonstrated beyond reasonable doubt that the supervisory authorities not only lack officials with the expertise and knowledge of insurance...but are also subject to red tape..."(ibid).

5.3.2.5 The Nigeria Reinsurance Corporation Decree 1977

In April 1976, the Military Government inaugurated the Financial System Review Committee to examine, the structure and adequacy of the Nigerian financial system, as well as the organisational and ownership structure of institutions within the system, with a view to evaluating their relevance and viability in the context of the Nigerian economy. The Committee submitted their report to government on the 23rd of December of the same year. As part of its recommendations, the committee proposed the following:

(1) the establishment of a National Reinsurance Corporation whose prime objective would be to focus on the development of a national reinsurance market. It recommended that the corporation should "concentrate its efforts on developing the reinsurance market in Nigeria but should not aim at regulating the industry".

The military government accepted these recommendations.

(2) the monopoly of Government business enjoyed by NICON "should be revoked in the light of the further Nigerianisation of the equity of foreign owned insurance companies in the country".

The military government rejected this recommendation,[121]giving no reasons for its decision. However, it accepted the Committees recommendation that NICON "...should...be treated by the Government as the lead company and should take on leadership responsibilities within the industry."

(3) part of the equity of NICON (which was fully federal government owned) should be offered to the state governments.

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121. One of the reasons government had given in respect of it's decision to participate directly in the market was the fact that the market was dominated by foreign insurers. Since this had been dealt with somewhat by the provisions of the Indigenisation decree, in principle, there was no reason for government to continue its operations in the market.

The government rejected this recommendation, stating that "...State Governments are free to go into insurance business subject to satisfying the necessary conditions under the Decree."

(4) the discriminatory tax provisions under section 16 of the Income Tax Management Act 1961 relating to the taxation of insurance companies pensions funds should be reviewed.

The Government accepted this recommendation.[122]

(5) A board with powers invested in it under the Insurance Decree should be established by the Ministry of Trade to regulate the insurance industry.

The Government rejected this recommendation, stating that it did not see the necessity for setting up another body in addition to the Ministry of Trade to regulate the industry.[123]

The Committee had apparently had knowledge of the Government's intention to raise the capital requirements for entry into the industry. In the report, it "fully endorsed" the Governments decision to raise the capital licensing requirements in life business to ₦300,00. In the 1976 Decree the capital requirements for life business was in fact raised to ₦500,000.

Subsequently, in 1977, the Federal Government promulgated the Nigeria Reinsurance Corporation Decree.[124] The decree was passed in keeping with the policy of localisation and domestication in the economy at the time and was deemed to have come into effect on the 1st of July 1976. It provided for the establishment of a corporation, The Nigeria Reinsurance Corporation[125] (or Nigeria Re as it came to be known), with an initial authorised share capital of ₦10,000,000. The functions of the

122. Although government accepted this recommendation, up till the time of writing, nothing has been done to redress the situation. Ogunshola (1976/7,p.84) noted that representations had in fact been made to the Federal Ministry of Finance by the Nigeria Insurance Association and the Life Offices Association as regards this problem,"...but each approach has been met with blunt refusal."

123. See Federal Military Government's Views on the Report of the Committee on the Nigerian Financial System, 1977 Federal Ministry of Information, Lagos, pp.21-24.

124. Otherwise known as Decree Number 49 of 1977.

125. Section 1.

Nigeria Re were set out in section 2 of the decree, that is, the reinsurance of all classes of insurance business including life insurance business, both within and outside Nigeria, among other things. Every registered insurer was required by the provisions of section 7 to reinsure with the corporation 20% of the sum insured on every insurance policy issued or renewed by it on or after the 1st of January 1978. Additionally the insurers were required to pay to the Nigeria Re 20% of the premium received on such policies.[126] The Nigeria Re in turn was required to pay the insurer's commission at a rate determinable by the corporation, although no profit commission was payable on such cessions.[127] The Nigeria Re also had the right of first refusal over any reinsurance business over the legal cessions before such business was placed on the international reinsurance market.[128] Since some of the functions of NICON were in effect transferred to the Nigeria Re, sections 4(2)(c), 8 and 9, as well as schedule 2 of the National Insurance Corporation of Nigeria Decree 1969 which dealt with reinsurance, were repealed by section 7(5) of the Nigeria Re Decree. The corporation was also charged with the responsibility for ceding compulsory cessions from Nigeria to the African Reinsurance Corporation. In addition the Nigeria Re was to "...create a focal point for the collection of market statistics,"[129] and carry out insurance market research activities. The Nigeria Re, as with the case of NICON was also granted discriminatory tax concessions.[130] It has been estimated that for the year 1988 alone, the effect of the tax limitation clause (with respect to the operations of the Nigeria Re) has been to deny the government of some ₦3.2 million in tax revenue (Naiyeju, 1990,p.8).

However, while the government had accepted the recommendations of the Financial Review Committee that the Nigeria Re should focus on the development of the reinsurance market, and leave regulation to the Insurance Department, in its official publication, The Nigeria Insurance Year Book, the corporation states;

> The Insurance Department of the Federal Ministry of Finance and Economic Development is responsible for the Control of the activities of Insurance Companies so as to ensure compliance with the

126. Because it was impracticable for the Corporation to participate in every life policy, it decided to compel life insurers in the market to cede compulsorily 25% of all life insurance treaties. It exercised it's right of first refusal on any facultative cases. The Nigeria Re increased it's participation on treaties to 40% with effect from 1st July 1986. See Osoka (1990,p.7).

127. Section 7(2).

128. Section 7(3) and (4).

129. "Ten Years of Professional Insurance in Nigeria", p.51.

provisions of the Nigerian Insurance Decree 1976 and other relevant legislation and regulations touching upon the business of insurance in the country. The Department which is headed by an official known as the Director, is assisted in its responsibility in this regard by the Nigeria Reinsurance Corporation and the National Insurance Corporation of Nigeria. *These three institutions ensure that government policy in the field of insurance and reinsurance is complied with by members in the Nigeria Insurance Market*"(italics mine).[131]

5.3.2.6 Extent of Industry Influence on Regulatory Decisions

The extent of influence that the insurance market has had on the regulatory process appears to have varied with the political and economic developments in the country. In the early 1960's, the dominant insurers in the market were the foreign ones who influenced regulation to the extent that the controls on the market were loose. This benefited both the foreign insurers as well as the indigenous ones. When the country was under civilian administration, the views of the industry were solicited through the Nigerian Insurance Consultative Council, who it is reported were pleased with the provisions of the draft insurance bill.[132]

From the available evidence the conclusion can be drawn that the insurance industry as an entity did not have much of a say in the discussions that led up to the promulgation of the NICON Decree 1969 and Insurance Decree of 1976. After the decree was passed there was much dissatisfaction with many of its provisions among industry practitioners. A lot of the dissatisfaction had to do with the capital and other licensing requirements as regards entry into the market. Some considered that the capital requirements were unnecessarily high, while others felt they were too low. The restrictions on investment behaviour were also criticised.[133] Indeed, during this period it appeared that the extent of industry influence on the public decision making processes that ultimately affected the operations of the insurance market was minimal. There was talk in the industry and within official Government circles as to making

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130. See section 4(2) of the Nigeria Re Decree.

131. See Nigeria Insurance Yearbook publications, various issues, for example 1989, p.186.

132. See Reichel (1966-1971) op.cit.,p.256.

133. See for example, Ogunshola 1976, Falegan 1982(d), Ojo and Adewunmi 1982 and Akintola-Bello 1983.

amendments to the decree.[134] However, it appeared that this process was shrouded in some degree of secrecy.

In 1979, the Military Government handed power to the civilians and the country was once again ruled under a democratic system of Government. During this time however, there was no regulatory action with respect to the insurance industry. At the end of 1983, the military administration swept themselves back into power after allegations of fraud, corruption and financial mismanagement on the part of the civilian administration. The change in government did not appear to have resulted in any significant changes in terms of increasing the influence of the industry on the regulatory body.

At the annual meeting of the Nigeria Insurance Association in 1985, the Chairman, in an address to members stated that the Governing Council of the association had submitted to the Insurance Department, its comments on the proposed amendment of the 1976 decree. He stated that the Council had unsuccessfully been trying to obtain from the Department information as regards when the proposed amendments would be put into effect.[135]

Similarly, at the First National Workshop on Life Assurance in 1986, the Chairman of the Education Sub-Committee, who also happened to be the senior manager in NICON's life insurance department, commented on the need of the Nigeria Insurance Association to make representations to the Government as to the desirability of raising the amount of tax relief allowable on life assurance from ₦2,000[136] to ₦10,000.[137] This issue had been raised repeatedly, because with the extremely high inflationary trends in the economy, ₦2000 Naira was a highly inadequate amount to serve as an inducement to life insurance purchases.[138] The possibility of the government increasing the amount allowed on investment in property by life offices from 25% to 50% was also discussed, and the question of the discriminatory taxation

134. Information obtained during discussions with industry executives and an Insurance Department official during May to July 1991.

135. Address delivered by Mr.J.S. Bedi. See Journal of the Insurance Institute of Nigeria, December 1985,p.9.

136. This was the amount prescribed the Income Tax Management Act of 1961.

137. Report by Chiejina, E.O, 1986, Chairman in Life Insurance, a half yearly journal of the Life Offices Committee.

138. The consumer price index had risen from 7.41 in 1961 to 105.3 in 1986. By 1991 it had risen to 259.65 (1985=100) (International Financial Statistics Yearbook 1991,p.568).

of life offices was again raised.[139] However, up to the time of writing, the requested amendments to the Decree had not been made.

According to the Insurance Department, the insurance industry participates in public policy making directly relevant to the insurance industry to a very large extent. The Insurance Department is said to arrange for meetings with industry representatives who represent the industry on various Government committees, in order to hear the representatives' views on regulation of the industry. Indeed in 1981, when the country was still under civilian rule the Insurance Department met with "leading" insurers in the industry to discuss ways in which the 1976 Insurance Decree could be amended, and in 1983, in response to the decision of the Government to lower the registration requirements in respect of all classes of insurance business, the various groups in the industry moved to stop this by exerting pressure on the government to pass a new act.

Discussions with a regulatory official in the Department revealed that the Department believes that the insurance industry is adequately represented in such discussions and that their input is taken into consideration when insurance laws are to be implemented. That the government holds consultations with some "representatives" of the industry is not in doubt.[140] It is (1) the extent to which such representatives are acting in the interests of all the member companies in the market, and (2) the extent to which the government takes into consideration the suggestions made and advice given, that is in question. Discussions with executives in some life insurance companies[141] between May and July 1991 reveal that their belief is that the government does not as a rule consult with the industry and when they do they seek the opinions of only a few "non-representative" bodies such as NICON and the Nigeria Re which are government corporations. A typical illustration given is that of section 5(1(f)) of the 1976 Act which requires that professionally qualified personnel be placed in charge of each department in insurance companies.[142] It is argued that if

139. Chiejina 1986, op.cit. p.5.

140. See, for example, Ogunlana (1985,p.34) who stated that "The...consultations which government has had on the proposed revision with representatives of the industry is to be commended as it will make for better legislation".

141. Interviews were held with the following executives:

Mr. Ope Oredugba, Managing Director, African Alliance Insurance Company; Mr. Willie Ezeogu, Senior Manager, American International Insurance Company; Mr Saka, Crusader Insurance Company; Mr. Femi Ajigbo, Crusader Insurance Company; Mr. Sola Thomas, Financial Insurance Company; Mrs Omope, Deputy Manager, Life Underwriting, Great Nigeria Insurance Company, Mr Adegbenle, Manager, Great Nigeria Insurance Company; Mr. Chiejinna, Life Manager, NICON. Full details of the method of these interviews have been provided in chapter one. See appendix B for the interview schedule.

the Government had actively solicited the views of those in the industry they would not have included this provision since it is well known that there is a shortage of professionally qualified personnel in the industry.

It indeed appears that with the 1976 decree at least, most of the private insurance companies in the industry were not actively involved in the formulation and discussion of the decree. The 1976 decree has been described as being

> "...relatively free from the frustrating influences of vested interests, [since it was]...an enactment of the federal military government...promulgated without debate or fanfare [and]...the antecedent formalities that would normally provide a legislative history for a civilian legislation" (Anifalaje 1984,p.88).

The evidence from the interviews held indicates industry dissatisfaction with some of the current regulatory rules. Nearly 50% of the executives interviewed stated their preference for less regulation of the market. The areas in which less regulation was desired were, not surprisingly, with respect to the investment rules, the life assurance premium relief and the taxation of the life fund. Three of them claimed to be in favour of increased regulation, but further discussion revealed that the areas in which they desired this were with respect to the supervision of life insurance intermediaries (many of who defaulted in remitting premiums to the companies) and the raising of the financial requirements for licensing new companies. A senior executive with access to the Director of Insurance said he had raised the issue of the necessity for the increased supervision of the intermediaries with the Director

> "...but nothing has been done and one gets tired of talking."

Another executive claimed that increasing the capital requirements would

> "...sort out the chaff from the grain."

The Insurance Departments apparent inability to supervise the industry in an effective manner was also a cause for concern. As one executive put it

> "should we make...regulations that we know cannot be supervised?"

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142. Section 5.

There are many interest groups in the market with varying degrees of "power". Their power appears to be dependent not only upon their financial resources, but also upon their status. Status in this case can be measured by the degree of close intimacy or personal relationships with members of the political elite, that is, those at the heart of the regulatory decision making process.[143] The various interest groups can be classified along the following lines;

(1) The big national companies such as NICON and the Nigeria Re.

(2) The big companies with some amount of foreign equity ownership.

(3) The "small fry,"[144] that is, the medium sized and small wholly indigenous owned companies.

(4) The consumers of insurance services.

The managing directors (in essence bureaucrats) of the national companies are appointed by the Government and it is to be assumed that they would have the advantage over the other companies in being able to influence public policy making. Being government appointees they would presumably be in close contact with the "powers that be" who, having no specialist knowledge of insurance would be inclined to rely upon their advice when contemplating legislative action in the industry. This is especially true since insurance is low in salience and high in complexity and in Gormley's (1986) regulatory framework this leads to a situation in which policy making is dominated by a "power elite" made up of bureaucrats, professionals and business groups in the industry. Apart from this it is the bureaucrats in the national companies that can be perceived as playing a dual role: they are government employees and yet at the same time they are professional people. In some cases these two roles could be conflicting.

However, the extent to which the bureaucrats in the industry (which term includes the Director of Insurance, the heads of the national companies and the heads of all Committees in which decisions pertaining to the insurance industry are taken) can influence the scope and nature of regulatory rules is not clear. This is because

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143. See section 2.2.2 in chapter 2.

144. Small in terms of size of life premium underwritten.

although an appearance of a democratic decision making process is given by the setting up of committees, under military rule, in the final analysis, the political elite are the ones responsible for public policy making. The political elite consist of the Minister of Finance, as well as the Permanent Secretary in the Ministry of Finance, the Council of Ministers acting through the Secretary to the Government, or the Chief of General Staff. However when regulatory decisions are made

> "...it is not always clear whether it is the decision of the Council of Ministers or the singular decision of the President (conveyed through the Secretary to the Government) or the decision of an aereopagus headed by the Chief of General Staff...[and] contradictions [in the regulatory decisions] only illustrate the pathology of our financial and economic administration" (Okigbo 1988,pp.11&12).[145]

The medium sized and small companies in the market would probably only be able to make their views known via the market associations. This would have been the ideal medium through which these companies (including the foreign companies) could make their views known and felt. However, lack of cooperation among the companies has to a large extent reduced their ability to exercise some strength in this area. For example, it was not until 1986, 27 years and 16 years after the formation of the Nigerian Institute of Insurance and the Nigerian Insurance Association, respectively, that statistics concerning insurers operations in the market could be complied and published.[146] Similarly, the progress of the Life Offices Committee of the Nigeria Insurance Association was slowed down considerably by politicking among member offices.[147] Therefore it was not until 1986 that the maiden issue of its journal, Life Insurance, was published, and it was in the same year that it held the first national workshop on life assurance.

The inability of some of the various market associations to work as a team (Ogunlana 1985,p.3) may have affected their ability to influence policy to some degree. For example, at the Insurance Department it is claimed that representations by the market for an increase in rates for some classes of business are not sufficiently supported by the requisite actuarial data, and as such have been refused.[148] This was confirmed by

145. This comment was made specifically with reference to the governments interventions in the banking sector, but are of relevance to the insurance sector, since both sectors are regulated by the Ministry of Finance.

146. The Nigeria Insurance Digest, published by the Nigeria Insurance Association.

147. Information obtained during an interview with the Chief Executive of African Alliance Co., a specialist life office, in July 1991.

148. Interview with Mr.J. Oni, Principal Actuary in the Insurance Department, 6th May 1991.

some of the executives interviewed who stated that the Life Offices Committee had been charged with the responsibility for presenting the life offices arguments to the Nigeria Insurance Association, who in turn were to present their case to the Insurance Department. However, they had been unsuccessful because they had not

> "...marshalled their points effectively..." and did "...not present their case to the [Insurance Department] adequately enough...."[149]

Another case in point is the question of mortality tables. The mortality table provides estimates of mortality probability at various ages and is the instrument by which the probability of living, or dying is measured. It forms the basis for determining the premium rates in life insurance (Magee 1952,p.27; Athearn 1977,p.404). Life offices make use of these tables to ascertain the probability of death occurring at each age for all policyholders and from this basis take into account other factors such as future interest rates and expenses in order to arrive at the price to be charged for the risk. Thus the mortality assumed is an important factor in determining the underwriting profitability or otherwise of the life portfolio. However, Nigerian life offices have been making use of British and American mortality tables[150] which may not be particularly suitable to Nigeria because of the different environmental conditions that exist. The mortality experience of the lives assured under various policies indicates that the mortality of European and Nigerian lives is different. The Life Offices Committee attempted to commence investigating the mortality experience of the various life offices but was unsuccessful in doing so.[151] The information obtained from the executives interviewed indicated that the lack of success in doing this was due to the lack of cooperation from member companies. All the life offices were requested to submit information on their mortality experience. In some cases, the request was ignored, and the requisite data not supplied and in other cases, was actually unavailable. This unavailability of mortality data precludes accurate computation of mortality experience and as such adequate and non-discriminatory rates.

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149. Quotations from interviews. The respondents names have not been given in this and subsequent quotations in order to preserve confidentiality.

150. The mortality tables in use in the industry at the time this study was undertaken were: The 1924/29 (A24/29) and 1949/52 (A49/52) U.K Tables; The 1953 and 1983 U.S Tables and the 1976 U.K Rate Book.

151. See paper presented by Akinwande, A.A., "The Insurance Industry in a Changing Economy-Opportunities and Challenges- Life Insurance Aspects", at the 20th Education Conference of The Insurance Institute of Nigeria, 1991,pp.18.

The reasons for the lack of cooperation among the life offices in the industry appear to be due to a combination of inefficiency (as displayed by the inability to supply requisite data) and some element of mutual distrust and suspicion (as evidenced by the unwillingness to supply data where available). However, there may be another reason. One very senior executive who had in the past, been a representative on the Life Offices Committee, believed that the efficacy of the committee had been sabotaged because it was becoming "too powerful". According to him this had been done by tampering with the composition of the committee so as to reduce their effectiveness and

> "Now the companies do not appoint senior level people to the committee with the result that the policy recommendations are not carried out. How do you expect an assistant superintendent to just walk up to his managing director and say 'this is the decision of the committee which is binding on the company'?. the managing director would not even bother to read the memo or listen to him! To make a thing like this effective, the managing director or someone who is powerful and can take decisions should be represented on such committees. I have never had any serious regard for their decisions."

It appears that public dissatisfaction with the activities of many insurers in the market, which has been voiced in strong criticisms of the industry, has influenced the Government's regulatory philosophy considerably. This is interesting because there are no organised consumer interest groups in the industry. The public perception of the activities of insurance companies in Nigeria is very bad,[152] especially in the case of the life offices. Consequently the regulatory trend has been on the side of stricter controls over the industry. A case in point is the reduction of motor rates in 1975, after strong pressure from consumers and despite strong resistance from insurers.

5.3.2.7 The Insurance (Special Provisions) Decree 1988

Life insurance has been a particular source of grievance for many policyholders. The agents selling these policies have been accused of all sorts of sharp practices and consumers have complained about the difficulties and delays associated with claims settlement.[153] These allegations are sharply refuted by the industry. The Chairman of

152. Nigerians have never been enamoured of the activities of insurance companies in the country. The Risk Bearer, 1988, Vol.13, No.13 p.5, states that "...it must be admitted that the Nigerian insurance industry does not enjoy ...public goodwill..."

153. See for example, Aigbe 1982, for a criticism of the life insurance industry in Nigeria and an overview of public attitudes towards life insurance.

the Life Offices Committee in an address to the First National Workshop on Life Assurance stated that

> " I can confirm that in all straightforward claims, the insurer settles claims with the minimum of delay...the Director of Insurance seldom complains of any malpractice by a life insurance company. In fact I do not know of any member of the Life Offices Committee that has received a letter of reprimand from the Director..."[154]

Despite the strong reassurances given by the chairman of the Life Offices Committee about the activities of the life offices, in 1988 the government promulgated the Insurance (Special Provisions) Decree 1988. The decree was divided into 11 short sections dealing with the subjects of disclosure of information on proposal forms, warranty and conditions, assignment of life policies, and third party rights against the insurer, amongst other things.

Again, the focus of the legislation was on safeguarding policyholder interests, and some portions of it generated some controversy in the industry. The controversial provisions of degree however was in respect of disclosure,[155] and "Insurable interest in life or other Insurance."[156]

Section 1 stated that it was the insurers responsibility to ensure that all questions on the proposal form were drawn up in such a way as to elicit all the information that the insurer considered material[157] to the risk, and that any information not requested specifically would be deemed to be immaterial to the risk to be undertaken. This understandably was not well received by the insurers in the market, who felt that although such a provision was suited to the British market,[158] it could not be applied to Nigeria since there was a great likelihood of proposers deliberately concealing facts

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154. Odele, M.O., 1986,"The Purpose of Life Assurance Claims and Settlement", Life Insurance, Vol.2/86,p.25

155. Section 1(1) to 1(4).

156. Sections 3, 4 and 5.

157. In insurance a material fact is defined as fact which would influence a prudent underwriter in making a decision as to whether or not to accept a risk, or if he decided to accept it, a material fact would influence his decision as to the terms on which the risk would be underwritten. The onus of proving whether a risk was material or not was originally on the policyholder whose responsibility it was to disclose all facts material to the risk whether or not he thought it was relevant at the time, or whether or not he was even aware of the existence of the fact considered to be material. As a result many insurers were able to deny liability on the grounds of non disclosure of material fact to the detriment of many innocent policyholders. The change in law would make this course of action very difficult for insurers in the future.

material to the risk, to the detriment of the insurers. Added to this was the fact that although life insurers sent their proposers for medical investigations before issuing life policies, the investigations, due to the limited sophisticated medical equipment on the market, might probably not reveal terminal illnesses in the early stages.

Although the industry was aware that a decree was to be passed, it is unlikely that the industry knew that such a provision was to be included in the decree. Even if it had been aware that this legislative provision was to be made, the evidence suggests they were unable to influence the policymakers in their favour. The Managing Director of the Nigeria Reinsurance Corporation who, as the head of a prominent national company, would be expected to have been consulted about the provisions of the new decree, had this to say;

> "It beats the imagination how the insurer can reasonably be expected to know all the material circumstances surrounding each and every risk that may be presented for cover...it affords the insurance consumer in Nigeria today a great deal of room to manoeuvre and hold the insurer to ransom..."[159]

The Nigeria Insurance Association were aware of the provisions in the draft bill relating to insurable interest and had made comments and suggestions regarding this aspect to the authorities.[160] The insurable interest provisions in effect extended insurable interest beyond members of the nuclear family to members of the extended family to take into account the socio-economic factors in the society and would, if nothing else, probably increase the amount of individual life business underwritten in the market.[161] These provisions would satisfy consumer interests because they took into account cultural and religious factors in the environment.

For example, now, unlike the situation before the Decree came into force, a man with four wives could name all four as beneficiaries under his life policy. A father could also have a life policy issued in respect of his son's life since he could argue that he

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158. This provision is made in the British Statement of Insurance Practice.

159. The Daily Champion, Wednesday May 22, 1991,p.4.

160. The Nigeria Insurance Digest 1986,p.25.

161. It has been suggested that this section of the decree is unacceptable in the sense that it completely rewrites the whole definition of insurable interest, which definition is international, and cannot or should not be rewritten to suit individual country conditions.

was or would in the future be financially dependant upon him. Again in situations where persons were not closely related to each other, one party could benefit as beneficiary under the others policy once he could prove that he was his dependant. These provisions considerably extend the life insurers potential claims liability.

Once again, the consumer interest appeared to have been the decisive factor behind regulatory action, and an industry commentator observed that the decree "...is not the darling of many insurance executives who argue that it only seeks to protect the insured at the expense of the insurer.[162]

5.4 The Structure of the Insurance Department

Currently, the Federal Government controls the activities of insurance companies in Nigeria through the Federal Ministry of Finance and Economic Development. The Insurance Department of this Ministry is charged with the responsibility of supervising the market activities and ensuring that the relevant regulations are complied with. The Insurance Department is headed by an official known as the Director of Insurance who is directly responsible to the Minister for Finance and Economic Development. The Director is appointed by interview and appointment in accordance with civil service guide-lines. The Insurance Department is supposed to be assisted in its functions by NICON and the Nigeria Re. Their stated function is to "ensure that government policy in the field of insurance and reinsurance is complied with by members in the Nigerian Insurance Market."[163] The Director of Insurance is assisted in his functions by the Deputy Director. Two Assistant Directors for Insurance and Audit in turn report to the Deputy Director (see figure 5A).

5.4.1 Staffing

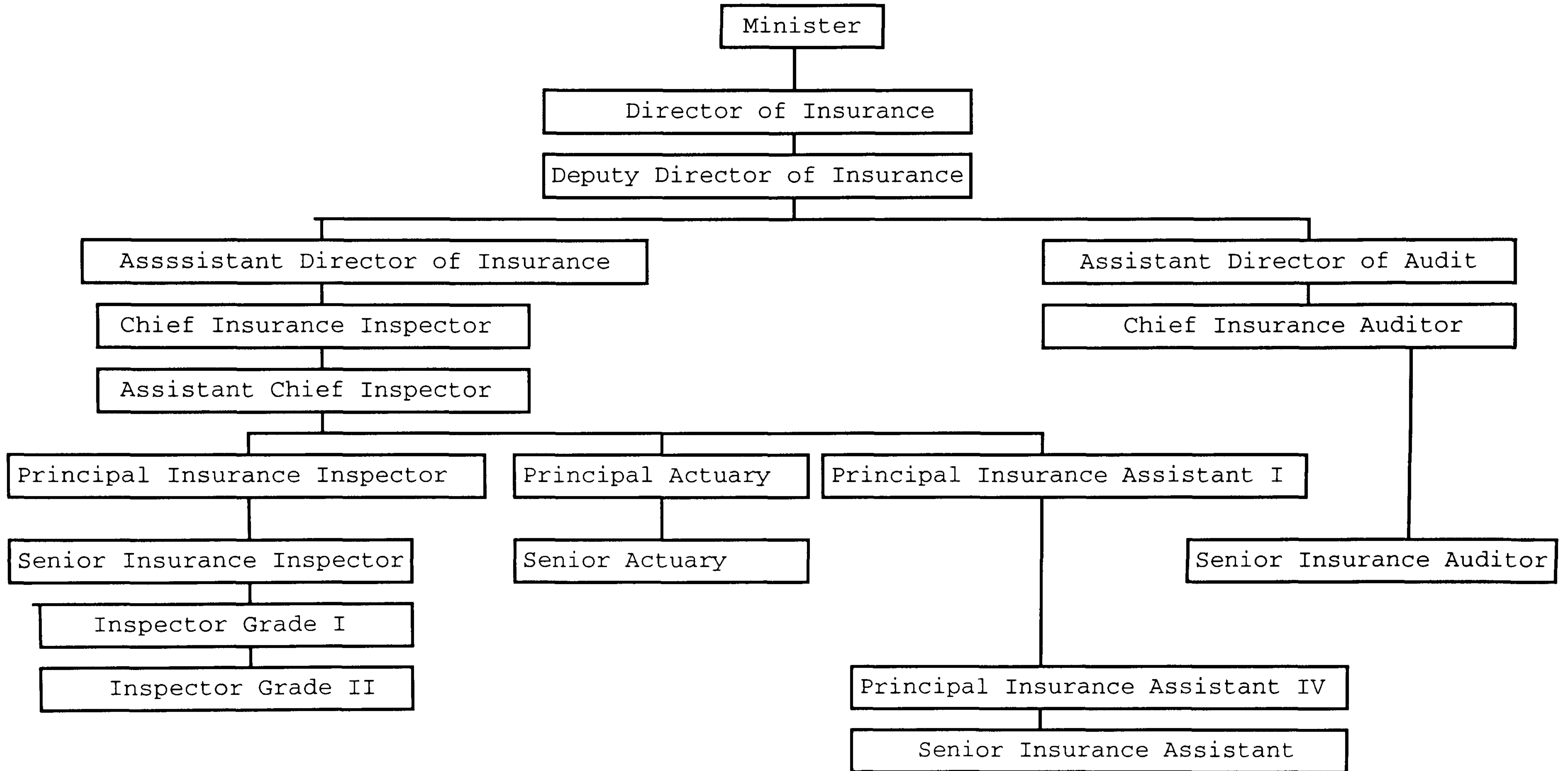
The agency staff are classified along two categories, the professional and administrative cadres. Civil service appointment rules govern the recruitment of agency personnel. At the time that the interviews were conducted there were about 150 staff in the Insurance Department.[164] Out of this number, 28 were graduates of Universities. Among these were two statisticians, one lawyer and two economists.

162. The Business Times, Monday August 27, 1990,p.19.

163. The Nigerian Insurance Year Book 1989,p.186.

164. The information in this section has been obtained from the Insurance Department.

Figure 5A
The Structure of the Insurance Department



There was no professionally qualified actuary in the department at this time. In fact in the 1960's and early 1970's there were no professionally qualified actuaries in the insurance market, and as such insurance companies employed the services of foreign actuaries in order to obtain their actuarial support (Adeyemo 1972,p.101).

The situation has changed somewhat in recent years with the emergence of a few (four) locally based actuarial consultants, although the majority of insurance companies however still employ the services of foreign actuarial firms.[165]

The Principal Actuary in the Insurance Department, although a mathematics graduate from the University of Lagos, was not professionally qualified.[166] All the university graduates are in the professional, that is, senior cadre. The Department is short-staffed at the professional level (Okwor 1982,p.19; Anifalaje 1984,p.92).[167] This apparently has been the situation since the Departments inception. In the 1960's and early 70's, the Office of the Superintendent of Insurance (as it was then called) was "thinly staffed", despite concerted efforts to man it with technical experts (Olawoyin 1976,p.64). Only staff at the professional level are involved in public policy making. Staff turnover is very high due to the poor conditions of service in the civil service. The staff that leave usually do so to take up jobs in the banking, oil and most especially insurance sectors in the economy, where far better pay and conditions of service obtain. Very few experienced personnel come in from the private sector to work in the Department.[168] The few that cross over usually do so at the higher professional` levels after they have made their money in the private sector. Morale among agency staff is low especially among the professional cadre whose salaries as

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165. See The Punch July 18 1989,p.10.

166. There is an acute shortage of professionally qualified actuaries in the Nigerian Insurance Market. The term "professionally qualified" presupposes that the individual has taken and passed the relevant examinations of approved institutes (usually those of the U.K and U.S.A). Since actuaries are scarce and highly paid, it is very unlikely that given the salary structure in the civil service, any qualified actuary would work in the insurance department. Even the private sector companies have difficulties in attracting and retaining actuaries. One company interviewed, The American International Insurance Co., had sent staff abroad for actuarial training. Upon completion of training, the staff did not return to the company or indeed the country presumably because of better conditions of service abroad.

167. For example, Anifalaje (1984,p.92) stated that "Although the state has admirably insisted on the thorough supervision of insurance documents in order to ensure that they are reasonable, fair and just and has charged the Director of Insurance with the onerous duty to execute supervision, regrettably it has not sufficiently provided the Director with the wherewithal for the effective discharge of this function." The Principal Actuary in the department confirmed this in an interview in May 1991.

168. Information obtained from The Insurance Department.

compared to the private sector insurance companies and other financial institutions are not competitive.[169]

5.4.2 Public Policy Making

The potential costs/benefits of insurance laws to the industry and/or consumer are not assessed in economic terms because the Department does not have people who are qualified to assess them. According to a source,[170] the bulk of the people in the Department are "liberal arts people who just talk and talk" and who do not have the competence to evaluate the probable effects of potential legislation. Policing or checking for compliance with laid down rules is done (in theory) by carrying out random investigations. These random investigations are carried out in cases where (1) there are complaints from members of the public (2) there are inadequate subsisting insurance treaties and (3) the actuarial valuation reports etc do not come into the department by the 31st of May of each year as required by law. The procedure for investigation is as follows. The Department writes to the company concerned asking for an explanation for the existence of a particular state of affairs. The Department having received this letter writes a report and sends it to the Director of Insurance. If the offence is grave enough to warrant an investigation, the Director asks the Department to investigate or, in some cases, the file may be sent to the legal department for immediate legal action in the courts. The Department does not particularly want to be involved in litigation because of the expenses involved in such actions. Lawyers have to be engaged and sent to the particular state of the federation in which the erring insurance company is headquartered since action must be brought against the insurance company in its area of jurisdiction.

5.4.3 Difficulties in Implementation of Regulatory Laws

The main difficulties said to be experienced by the agency in the implementation of regulatory measures are in the following areas:

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169. The significant difference between private sector salaries and emoluments and the public sector salaries in Nigeria is common knowledge. See The Business Times, Monday July 23 1990,p.10.

170. To preserve confidentiality the source will not be named. The Interview took place during the period May to June 1991.

(1) non-remittance of outstanding premiums from insurance brokers and agents to insurance companies,

(2) non compliance with the requirements in the decree regarding the submission of actuarial valuation reports. Since there were until very recently no professionally qualified actuaries in the country, insurance companies sent out their life statistics abroad to actuaries who were paid for their professional services in foreign currency. With the advent of the Structural Adjustment Programme (SAP), this process was made increasingly difficult because insurance companies found it more difficult to obtain foreign exchange as a result of the increased cost of foreign currency. The companies began to procrastinate and send in portions, rather than the whole of their returns. Since the Insurance Decree of 1976 and other legislation in force are silent about the partial submission of returns, the regulatory department in such cases cannot penalize a company so long as it submits a part of its returns. Since the life offices send their reports abroad, the actuary's report usually comes in a year or so later than the official deadline.

(3) complaints from consumers about the arbitrary repudiation of liability on the part of insurers, differences as to the quantum of the sum offered as compensation to policyholders, and sharp practices among insurers such as charging more than the tariff for excesses,

(4) the operations of NICON which have been described by a regulatory official[171] as "a headache and...lax and inefficient."

5.4.4 Record Keeping

The systems of record keeping and record retrieval at the insurance department at the time of the study were found to be poor and rudimentary.[172] Statistics of insurance company operations, where available, were recorded on ruled, A4 size sheets of paper and filed in file jackets. Entries were made with ballpoint pens or pencils and in some cases were incomplete.[173] The statistical information did not go back very far: the

171. This comment was made by a regulatory official at the Insurance Department.

172. These observations were made during visits to the Insurance Department during the period May to June 1991.

173. It was not clear whether the omissions were as a result of the submission of incomplete data on the part of some insurance companies, or whether they were due to filing errors made by administrative personnel in the Deparment.

earliest data for the companies was found to relate to 1974. The Department did not make use of modern record keeping and retrieval systems such as computers. The Government had previously voted a specific amount for the computerisation of the Department, but the usual bureaucratic delays for which the civil service in Nigeria is characterised had prevented the systems from being set-up. Some of the data regarding the returns of insurance companies were unavailable. According to the agency, this was mostly due to some companies either not submitting returns or submitting incomplete returns.

Summary

The stated primary objectives of insurance regulation in Nigeria are:

(1) the protection of the consumer interest and

(2) the development of a strong local insurance and reinsurance market in keeping with the country's development aspirations.

Over the years, these objectives have been implemented in two ways:

(1) the development of industry specific rules and regulations and

(2) the implementation of general economic policy that affects the insurance sector.

The regulatory philosophy has shifted over the years from one of relative freedom of operation in the market to a system of close supervision of insurance business. Restrictions have, over the years, been placed on the insurance market on a services and establishment basis. The original emphasis of regulation was on the licensing of insurance companies, but gradually the stated intention of regulation moved to that of achieving the localisation of insurance business with a view to increasing the retention capacity of the local insurance industry as evidenced by the establishment of NICON and the Nigeria Re.

In the early 1960's the Government did not have specific policy as regards the role that life insurance would be expected to play in the economy. In general there was no clearly defined policy specific to the insurance sector of the economy. As a result the Government's legislative action in respect of the industry was reactive, rather than

planned or anticipatory. However, as successive Governments began to plan the pace and nature of development of the economy, the insurance sector was seen as a potential generator of development capital in the economy. The NICON and Nigeria Re Decrees were promulgated as part of governments general policy of domesticating the Nigerian economy and reducing the country's reliance on foreign goods and capital.

Regulation had over the period been the province of government departments in the Ministry of Trade and then the Ministry of Finance and Economic Development. The regulatory apparatus has been characterised by the problems of a bureaucratic machinery. The Insurance Department is perennially understaffed (in terms of professional people) and morale is low due to the poor conditions of service, among other factors. Additionally, and perhaps not surprisingly, the Department has problems with policing and ensuring compliance with regulatory measures. Apart from this the department is not independent, and under military administrations especially, it does not appear to have a significant degree of decision making power. It is simply a place to which insurance companies are expected to make returns on their activities. The actual determination of public policy with respect to insurance is done by the political elite who are advised by the civil service. The extent to which such advice is taken is debatable, but the general industry feeling is that it is insignificant.

It appears that in the early years, industry views and opinions were solicited and incorporated in the formulation of regulatory policy. This resulted in ineffective legislation which at the time was in the interests of the foreign dominated insurance market. Over the years, with changes in the political landscape in the country, among other things, it appears that the interest groups in the insurance industry have not been able to significantly influence the nature of regulatory philosophy which has been determined in part by the needs and aspirations of the country as perceived by national development planners. Regulatory policy affecting the industry can be classified along two lines, insurance industry specific legislation and general economic policy. It is clear that in the 1970's, the regulatory philosophy of the Government in terms of the domestication of insurance business was driven by the general economic policies that have been implemented over the years. To the extent that recent economic policy is being dictated by external forces, there have been spill over effects in the insurance industry. Evidence of this can be is the recent moves to deregulate the economy which has resulted in government withdrawing from it's participation in some insurance companies.

The apparent inability of the insurance industry to influence regulation is also evident in the fact that although representations have been made to the government, through the Insurance Department, for the amendment of certain provisions in current laws, this has not been done.[174] The lack of cooperation among the various insurers in the market in the past is also a contributory factor.

It appears that public opinion in the form of dissatisfaction with the conduct of insurers has also influenced the nature of industry specific regulatory changes in the favour of the consumer interest. How this has been achieved is not clear. The activities of fraudulent and inefficient companies has, however, been extensively reported in the news media and it is conceivable that there are close interpersonal relationships between some consumer groups and the political elite.

The interest groups do not support regulation that they consider is not beneficial to their interests. For example, the requirement for a competent and professionally qualified man to run each department in an insurance company was not well received because it would among other things, increase the costs of operation. Similarly the provisions relating to disclosure in the 1988 decree, although in the policyholders interest, was not acceptable to industry groups.

However, while the intent of regulatory laws may be adduced from the contents of the regulatory instruments and statements made by key public officials, the only way in which the effectiveness or otherwise of the laws may be ascertained is by examining industry structure, conduct and performance over the relevant period. This issue is addressed in the next chapter.

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174. For example the tax laws on premium relief and discriminatory taxation between life office pension funds and uninsured funds.

Chapter 6

Nigerian Life Insurance Industry Structure, Conduct and Performance 1960-1988

Introduction

Economic theory suggests that the structural features of an industry influences the behaviour of firms and the prices, costs, profits and innovative activity resulting in the market.1 The structure-conduct-performance hypothesis emphasises a causal relationship between market structure, conduct and performance. This model of industrial organisation provides a background against which industrial organisation and behaviour may be analysed.

The traditional model postulates that the firms market structure affects its conduct which in turn affects firm performance. Market structure refers to the characteristics of the organisation of a market that seem to exercise a strategic influence on the nature of competition in the market. The salient aspects are:

(1) The degree of seller concentration which is thought to play an important part in determining business behaviour and performance. Economic theory and observation suggest that the character, intensity and effectiveness of competition among sellers is significantly influenced by this factor. Thus its degree of presence or absence within the market could be said to be an indication of the degree of competition or otherwise present. A high degree of concentration is an indication of increasing levels of monopoly power.

(2) Barriers to entry which include economies of scale, absolute cost advantages of established entrants over new ones and the degree of product differentiation among various sellers. The existence of significant levels of economies of scale is thought to support increasing levels of industry concentration which results in the considerable exertion of market power by larger firms.

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1. See for example, Bain 1968, Koch 1974 and Shepherd 1985.

Market conduct emphasises the behavioural patterns that firms within an industry adopt in response to the nature of the markets in which they sell or buy. It includes such features as pricing and advertising policies adopted with respect to other competitors within the industry. Performance is reflected in the composite of end results which firms in any market arrive at by pursuing whatever lines of conduct they have chosen and is reflected in the price-cost and profit patterns, technical efficiency and the rate of technological progress of the industry.

The acceptance of the structure-conduct-performance model is not unanimous and the direction of causation may not be one, but two-way because conduct and performance may also affect market structure. For example, tactics adopted by firms such as predatory pricing and frequent product style changes may drive competing firms out of the market which may subsequently alter market structure.

In this chapter, relevant data from the Nigerian life market are examined in an attempt to analyse the changes in market structure, behaviour and performance during the 1960-1988 period. It has been established earlier that reliable data on insurance company operations in general for the pre-independence and indeed some of the post-independence periods are generally non-existent. Additionally the practice of life insurance business did not begin until the 1960's long after the inception of non-life business.[2] Therefore for the purposes of the analysis in this section, most of the company data utilised is from 1968 since it is from this period that some reliable data as regards life company operations are available. The data on insurance company operations for the years 1968-1974 were not available at the Insurance Department as at the time of research.[3] As a result official data from sources such as The Central Bank of Nigeria, in respect of these years will be used. These data are reliable to the extent that they were originally obtained from the Insurance Department when these records were available at the Department. In order to obtain a complete picture, it has also been necessary to use, to a limited extent, data obtained from the Annual Abstract of Statistics[4] as well as from some secondary sources. Although some of the data are inconsistent across the various data sources, the differences are not expected to detract from any conclusions made in this section.

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2. See section 5.2.1.

3. No explanation could be given for this state of affairs. The conclusion to be drawn from this is that the files containing the relevant data had been "temporarily" misplaced.

4. This is published by the Federal Ministry of Information, Lagos.

The data for the period from 1977-1988 are not subject to such limitations as they were available at the Insurance Department. The decision to restrict the range of analysis to the year 1988 is due to the non availability of the requisite data beyond this year. As a result of the problems with the collection of and compilation of data on insurance market operations, there is an unreasonable time lag before the statistics are published. The statistics are not published by the Insurance Department, but by the Research Department of the Nigeria Re who obtain the data from the Insurance Department. Often the data available are incomplete. While the Insurance Department blames the insurance companies for not submitting returns within regulatory requirements, the companies claim that the returns for the most part are submitted on time but that the agency is very slow in compiling the data.[5]

Within the limitations stated above, the effects of regulation on the structure, conduct and performance of some aspects of life insurance operations will be considered. It has been established that the regulatory objectives with respect to the life market are:

(1) policyholder protection

(2) the strengthening of the local insurance and reinsurance market

(3) the contribution to the economic development of the nation.[6]

In order to determine whether (or to what extent) these objectives have been attained specified structural and behavioural aspects of the market will be examined. In addition to this, some performance indicators which have a direct bearing on the attainment of these objectives are examined in the following sections. The analysis will be done in two phases.

The first phase will cover the period from 1960-1976 (1976 being the year when the 1976 decree, the most comprehensive piece of legislation to date which governs insurance market operations, was promulgated) and the second phase will cover the period from 1977 to 1988. The rationale for studying these two periods is to compare

5. Mr. Eugene Okwor, the Director of Insurance has in the past, in an oblique reference to the Nigerian situation stated that "...there is a lack of [sic] up-to-date and accurate statistics of the operations of insurance companies", Okwor (1982,p.22). See also Ogunshola (1973,p.59). The situation has not changed much since then.

6. See discussion in chapter 5.

the prior market structure of the insurance market (the 1960-1976 period) with the existing market structure in the 1977-1988 period. A comparison of structure and behaviour in both time periods is expected to reveal shifts or changes in industry structure and/or patterns of behaviour. However, the problem lies in determining whether such changes have been driven by regulatory or other environmental factors. In an attempt to isolate the effects of regulatory change within the data constraints, time series and cross sectional analyses have been employed. The results of the analyses as well as the methodology employed are discussed in section 6.4.

The localisation policies of the Government have been motivated by the desire to strengthen the local insurance market by increasing it's capacity. The performance of the national, foreign and indigenous companies is compared in order to determine whether the rationale for establishing national companies, and restricting the operation of foreign companies, is justified by their market performance.

6.1 Regulation and Life Industry Structure and Behaviour 1968-1976

6.1.1 Number and Location of Firms

The number of registered companies underwriting insurance between 1968 and 1974 is shown in table 6.1. These figures are inclusive of life and non-life business. Because of the non availability of data in the period from 1960-1968, the exact number of companies operating in the market at the time cannot be determined. Since the Insurance Act of 1961 and the Insurance (Miscellaneous Provisions) Act of 1964 were not enforced,[7] there were many unlicensed and undercapitalised insurance companies operating in the market.[8] The number of insurance companies in the market in 1960, 1963, 1967 and 1968 have been estimated at 59, 44, 67 and 88 respectively.[9]

According to the Office of the Superintendent, none of the companies operating in the market in 1967 and only one of the 88 in 1968 were registered under the Insurance

7. See sections 6.3.1 and 6.3.2.

8. See "Development of Insurance and Reinsurance in Nigeria" in 10 Years of Professional Reinsurance in Nigeria, at p.38, and also Agu (1986,p.3); Ogunlana (1972,p.37) Olawoyin (1976,p.64).

9. These figures were apparently given to Ajibola Ogunshola who was then the Life Manager of NICON by the office of the Superintendent of Insurance as it was then called. See Ogunshola 1973,p.57. The 1966 estimate is found in Adeyemo (1972,p.96).

Table 6.1
Registered Insurance Companies in Nigeria
1969-1974

Class of Bz/Year	1968	1969	1970	1971	1972	1973	1974
Life	3 (13.6)	6 (22.3)	7 (16.3)	6 (11.3)	8 (12.3)	9 (12.8)	9 (12.8)
Non-Life	11 (50.0)	13 (48.1)	26 (60.5)	38 (71.7)	43 (66.2)	44 (62.8)	41 (58.6)
Composite	8 (36.4)	8 (29.6)	10 (23.2)	9 (17.0)	14 (21.5)	14 (24.4)	20 (28.6)
Total	22(100.0)	27(100.0)	43(100.0)	53(100.0)	65(100.0)	70(100.0)	70(100.0)
Life & Composite	11 (50.0)	14 (51.8)	17 (39.5)	15 (28.3)	22 (33.8)	23 (37.2)	29 (41.4)

Source: (1) 1968 data Ojo & Adewumni 1982 (2) 1969-1974 Omoruyi & Demuren in CBN Economic and Financial Review 1980,p.28.

Companies Act. Fifty percent of the companies for which returns were available were underwriting life insurance business in 1968,[10] and although there was an increase in the number of these companies in absolute terms (11 in 1968 to 29 in 1974), the percentage of life companies did not increase as rapidly as those underwriting non-life business. In fact, the percentage decreased over the period to about 41% in 1974. (See table 6.1).

Almost all the principal offices of the registered companies were located in Lagos as at 1971 with a very small fraction having established headquarters outside Lagos (table 6.2). Lagos at this time, apart from being the capital city, was the financial and social centre of the country. It is expected that the insurance companies would be located here for ease of communications and geographical accessibility to overseas financial centres, among other things. This concentration in Lagos has continued to be the pattern[11] and it is from here that most of the total life funds are generated.

Table 6.2
Location of Nigerian Life Insurance Companies Principal Offices 1971

Class of Bz	Principal Office		Total
	Lagos (%)	Other (%)	
Life	7 (39.0)	1 (5.5)	8 (44.5)
Composite	9 (50.0)	1 (5.5)	10 (55.5)
Total	16 (89.0)	2 (11.0)	18(100.0)

Source: Adapted from Adeyemo 1972,p.97

6.1.2 Ownership of Life Offices

In 1965 and 1966, the number of exclusively foreign owned insurance companies in the combined life and general market was 78% and about 70% of the total population of offices respectively. If the number of companies with joint Nigerian/foreign ownership is taken into consideration, the percentages are higher, 92% in 1965 and

10. The reason behind the inconsistency between the 1968 figure in the table and that given by the office of the Superintendent of insurance lies in the fact that not all the companies in the market submitted their returns to the Insurance Department. In addition, the agency did not enforce compliance with the relevant regulatory requirements in this area. Aside from this most if not all of the insurance companies in the market were not licensed according to the provisions of the 1961 Act and as such were probably reluctant to submit returns so as not to draw attention to themselves.

11. See section 6.2.1 for more recent figures.

90% in 1966 (see tables 6.3(a&b)). At this time, most Nigerian insurance professionals did not have the requisite expertise to manage life offices on their own, and there were no legal restraints under the 1961, 1964 and 1969 (NICON) Acts as regards foreign ownership of business at this time.

The dominance of the foreign owned offices can be seen from table 6.3(b). At this time, about 32% of the life offices under exclusive foreign ownership controlled about 17% of the capital and 58% of the investment funds of the industry. About 79% of the companies were under joint Nigerian and foreign ownership and they controlled and owned 85.6% and 99.5% of the capital and investable funds in the life market respectively. The few purely indigenous life offices (21% of the life industry total) owned the least percentage of industry capital (14.4%) and investment (0.5%) funds.

Table 6.3(a)
Ownership Structure of Nigerian Insurance Companies 1965 & 1966

Company	Number of Companies		%Industry Share	
	1965	1966	1965	1966
Foreign	39	34	78	70
Joint	7	10	14	20
Indigenous	4	5	8	10
Total	50	49	100.0	100.0

Source: Adeyemo 1972,p.98

Table 6.3(b)
Ownership Structure of Nigerian Life Offices December 1971

Company	Number	%	% Industry Share	
			Capital	Investment
Foreign	6	(31.60)	17.4	57.9
Major	5	(26.30)	50.9	25.2
Minor	4	(21.05)	17.3	16.4
Subtotal	15	(78.95)	85.6	99.5
Indigenous	4	(21.05)	14.4	0.5
Total	19	(100.0)	100.0	100.0

Source: Ojo 1976,p.52

Table 6.4
Ownership Structure of Nigerian Life Offices 1969-1976

Class ofBz/Year	1969(%)	1970(%)	1971(%)	1972(%)	1973(%)	1974(%)	1975(%)	1976(%)
Life								
Foreign	4(28.6)	5(31.2)	4(26.6)	5(22.7)	5(19.2)	3(10.3)	3(11.5)	-
Joint	1 (7.1)	1 (6.3)	1 (6.7)	2 (9.1)	3(11.5)	4(13.8)	4(15.4)	5(19.2)
Indigenous	1 (7.1)	1 (6.3)	1 (6.7)	1 (4.6)	1 (3.9)	2 (6.9)	2 (7.7)	12(46.2)
Subtotal	6(42.9)	7(43.7)	6(40.0)	8(36.4)	9(34.6)	9(31.0)	9(34.6)	17(16.4)
Composite								
Foreign	6(42.9)	4(25.0)	4(26.6)	-	1 (3.9)	-	-	
Joint	1 (7.1)	1 (6.3)	1(6.7)	7(31.8)	7(26.9)	6(20.7)	5(19.2)	3(13.6)
Indigenous	1 (7.1)	4(25.0)	4(26.6)	7(31.8)	9(34.6)	14(48.3)	12(46.2)	13(59.1)
Subtotal	8(57.1)	9(56.3)	9(59.9)	14(63.6)	17(65.4)	20(69.0)	17(16.4)	16(72.2)
Total	14(100.0)	16(100.0)	4(100.0)	22(100.0)	26(100.0)	29(100.0)	26(100.0)	22(100.0)

Source: Adapted from CBN Review 1980,p29

The ownership structure of both life and composite companies during the period 1969-1976 (table 6.4) shows that between 1969 and 1976 while the percentage of foreign offices went down from 71.5% in 1969 to 4.5% in 1976, the percentage of joint Nigerian and foreign offices rose from 14.2% in 1969 to 27.3% in 1976. The decrease in the number of foreign offices followed the enactment of the Nigerian Enterprises Promotion Decree.[12] After November 1973 (when the Government decided to participate in the equity holdings of all viable foreign owned insurance companies in the country) the foreign companies began divesting themselves of their equity capital. By the time the 1977 Enterprises Promotion decree was promulgated, most foreign companies already possessed substantial indigenous capital.

6.1.3 Size of Market

The size of the market can be viewed from the following closely related perspectives;

(a) The gross premium income of the life offices for the period under review (table 6.5).

The annual growth rate of the life market during the period 1960-1976 was about 29%. In real terms however, the growth rate was lower (19.4%).[13] The market appeared to be growing up till 1966, after which negative growth rates were recorded. The market did not really pick up again until 1971, after the end of the 1967-1970 civil war, when an increase of about 54.4% (real terms) over 1970 premiums was recorded. The relative shares of the different classes of insurance business during this period are recorded in table 6.6.

(b) The percentage of the total insurance market which is attributable to life business.

122. See chapter four.

13. The Consumer Price Index has been used to deflate the life premium values since the GDP deflator for the years 1961 through 1972 are unavailable. The real premium figures are therefore slightly on the high side.

Table 6.5
Gross Premium Income of Nigerian Insurance Companies
1960-1974 (₦'000)

Year	Life Premiums	Growth Rates %	Real Life Premiums	Growth Rates %	Life (%Total)	Non-Life Premiums	% Total	Total Premiums
1960	618				(8.8)	6438	(91.2)	7056
1961	1054	(70.6)	142.2		(12.4)	7416	(87.6)	8470
1962	1332	(26.4)	170.8	(20.1)	(14.7)	7738	(85.3)	9070
1963	2624	(97.0)	345.7	(102.4)	(21.6)	9506	(78.4)	12130
1964	3828	(45.5)	499.1	(44.4)	(23.0)	12780	(77.0)	16598
1965	5238	(34.6)	644.7	(29.2)	(29.0)	12598	(1.0)	17736
1966	6478	(26.1)	741.2	(14.9)	(37.7)	10700	(62.3)	17178
1967	6030	(-6.9)	717.0	(-3.2)	(36.6)	10458	(63.4)	16488
1968	5322	(-11.7)	634.0	(-13.1)	(39.3)	8212	(60.7)	13534
1969	6402	(20.7)	694.4	(9.5)	(42.5)	8652	(57.5)	15054
1970	6852	(7.0)	653.2	(-5.9)	(35.6)	12384	(64.4)	19236
1971	12584	(83.6)	1009.1	(54.5)	(45.5)	15060	(54.5)	27644
1972	13878	(10.3)	1140.3	(13.0)	(47.1)	15585	(52.8)	29463
1973	15468	(11.5)	1228.6	(7.7)	(33.8)	30334	(66.2)	45814
1974	23592	(52.5)	1578.1	(28.4)	(37.2)	39749	(62.8)	63341
1975	25689	(8.2)	1283.2	(-22.9)	(20.8)	96803	(79.2)	123292
1976	34490	(34.3)	1386.3	(0.8)	(18.3)	154170	(81.7)	188660

Source of premium data: 1960-1968, Annual Abstract of Statistics, Lagos, various issues
(2) 1969-1974, Omoruyi and Demuren, Central Bank Financial and Economic Review 1980,pp30-31,
(3) 1969-1971 Total Gross Premium Figures, Annual Abstract of Statistics.

Table 6.6
Percentage Distribution of Various Classes of Insurance Business
1960-1976

Rank/Year	1960	1961	1962	1963	1964	1965	1966	1967
1	M (65.6)	M (62.5)	M (57.9)	M (48.8)	M (46.1)	M (43.7)	M (41.3)	M (40.9)
2	F (12.6)	F (12.4)	L (14.3)	L (17.2)	L (22.5)	L (29.0)	L (37.5)	L (35.4)
3	O (9.1)	L (12.0)	F (13.6)	O (10.3)	F (19.6)	F (15.0)	F (10.0)	F (10.9)
4	L (8.8)	O (10.1)	O (9.3)	F (4.1)	O (7.6)	O (8.4)	O (7.3)	O (8.8)
5	E (3.9)	E (3.1)	E (4.9)	E (3.0)	E (4.2)	E (3.9)	E (3.9)	E (4.0)

Rank/Year	1969	1970	1971	1972	1973	1974	1975	1976
1	L (42.0)	M (41.7)	M (41.9)	M (59.2)	M (46.3)	M (46.3)	M (40.2)	M (40.2)
2	M (37.0)	L (36.8)	L (38.8)	L (18.3)	L (29.7)	L (33.6)	L (20.8)	L (20.8)
3	F (9.4)	F (8.9)	F (7.9)	F (8.8)	F (9.3)	F (7.1)	F (16.8)	G (17.2)
4	O (7.2)	O (8.1)	O (8.1)	O (9.1)	O (9.8)	O (9.7)	G (13.0)	F (14.0)
5	E (4.4)	E (4.5)	E (3.3)	E (4.6)	E (4.6)	E (3.3)	A (19.2)	A (10.3)

Notes: (1) L, M, F and E denote life, motor, fire and employers liability and workmen's compensation insurance respectively, while O includes accident and miscellaneous insurance business. (2) 1960-1963 data based on net premium income (3) 1967-1976 data based on gross premiums.

During this period motor insurance was the most significant class of business underwritten in terms of percentage share of the total insurance market. Motor vehicle usage was on the increase and legislative provisions required that motor vehicle owners and drivers possess at least third party insurance on these vehicles.

From 1962 (with the exception of 1969) life business consistently contributed the second largest portion of total market premium income, although the size of the market appeared to be declining in comparison with the motor market.

6.1.4 Entry into the Market

The growth in the number of companies underwriting insurance business (life and non-life) during this period was very rapid. Since many unregistered companies were able to operate because of the lack of adequate supervision, it is virtually impossible to determine the number of companies in the market during this period. The registration requirements under the 1961 Act were relatively easy for the companies to comply with. There was no legislative provision for the establishment and maintenance of adequate free reserves and technical reserves, and no requirement for the companies to be managed by personnel with technical expertise. Thus there were very few financial and legal barriers to entry into the market.

Concentration in the life market (calculated on the basis of earning assets of the top 5 life offices) during the years 1969, 1972 and 1974 has been estimated at 85.5%, 81.3% and 64.0% (Agu 1986,p.9). The sharp decrease in concentration in 1974 may be attributed to the effects of the Indigenisation programme implemented by the Government. The foreign companies had monopolised industry premiums, capital and assets and the restriction of their operations led to a decrease in monopoly power in the market. During the 1969-1976 period, there was a total of eight entrants into the life market, with 1971-1972 and 1973-1974 being the most active years. More composite offices (13) than pure life offices (4) entered the market, probably because the successful operation of a pure life company required the availability of personnel with life insurance exposure and expertise which were scarce. This idea is supported by the fact that out of the six companies that exited from the market between 1970-1976, four were life and two composite. It could be said that on average, there were 2 new entrants each year. Specifically the rate of entry into the market was 2.13 offices per year, while the exit rate was comparatively lower at 1.13 per year. (See tables 6.7(a) & (b).

Table 6.7(a)
Nigerian life Offices
1969-1977

Year	Total	Life	Composite
1969	14	6	8
1970	17	7	10
1971	15	6	9
1972	22	8	14
1973	23	9	14
1974	29	9	20
1975	26	9	17
1976	22	6	16

Table 6.7(b)
Entry into the Nigerian Life Market
1969-1976

Year	Total Entry	Entry		Exit	
		L	C	L	C
1969-1970	+3	+1	+2	0	0
1970-1971	-2	0	0	-1	-1
1971-1972	+7	+2	+5	0	0
1972-1973	+1	+1	0	0	0
1973-1974	+6	0	+6	0	0
1974-1975	-3	0	0	0	-3
1975-1976	-4	0	0	-3	-1
1969-1976	+8	+4	+14	-4	-5

6.1.5 Intermediaries

The main distributors of life insurance business (as well as general insurance) were agents and brokers. The agents were salaried as well as commission agents. Some direct business was underwritten by the companies. The behaviour of insurance intermediaries has been discussed earlier on.[14]

The main product sold at this time was whole life insurance although term and endowment insurances were gradually introduced. The most popular life assurance product was the with profit endowment insurance policy (Ojo 1974,pp.269-272).

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144. See section 5.2.2.

The first attempt by the Government to control the activities of insurance intermediaries, specifically brokers, was by the establishment of NICON as a broker, underwriter and agent.[15] Although the effect of the control measure had a greater impact on the non-life market, the effect was also felt in the life sector, since all market intermediaries were perceived as inefficient and/or fraudulent. Public confidence in insurance business in general and life insurance business in particular was at a very low level.

From the registration pattern of life insurance brokers in Nigeria up till 1974 (the period for which data was available) it appears that the growth in the number of brokers operating in this market was quite slow, the most active period being between 1972 and 1974. The location of their principal offices follows a pattern similar to that of the life offices, the majority of brokerage offices (about 76%) being located in Lagos as at 1974 (tables 6.8(a)&(b).

Table 6.8(a)
Location of Nigerian Life Insurance Brokers Principal Offices 1974

Broker	Principal Lagos	Office Others	Total
Life	2(19.5)	-	2(90.5)
Life & General	14(66.7)	5(23.8)	19(9.5)
Total	16(76.2)	5(23.8)	21(100.0)

6.1.6 Investment Behaviour

Although data for the period 1960-1968 are generally unavailable due to lapses in the legal reporting requirements of the time, the position however, changed somewhat with the enforcement of some of the provisions of the Insurance Companies Act 1961, and the 1964 Provisions in the Insurance Companies Regulations in 1968. Table 6.9 shows the pattern of investment of the life offices for the period 1969-1974. Reliable figures for 1975-1976 were unavailable.

Life insurance companies in the course of their activities incur liabilities which are essentially long term in nature. In so doing, they generate a sizeable amount of premiums. Under the level premium system, the average life office receives it's

15. See section 5.2.2.2.2.

Table 6.8(b)
Registered Life Brokers in Nigeria
1955-1974

Class of Bz/Year	1955	1958	1960	1962	1964	1966	1968	1970	1972	1974
Life	-	-	-	-	1	1	1	1	1	2
Life & General	1	2	3	4	6	8	11	12	14	19
Total	1	2	3	4	7	9	12	13	15	21

Table 6.9
Nigerian Life Office Assets
1969-1974 (₦'million)

Assets	1969 (%)	1970 (%)	1971 (%)	1972 (%)	1973 (%)	1974 (%)
Government Securities	4.0(20.2)	4.5(18.7)	7.8 (26.5)	8.0 (25.4)	15.3 (26.9)	15.4 (25.1)
Stocks, Shares, Bonds	2.5(12.4)	4.1(17.2)	3.0 (10.0)	5.1 (16.2)	7.0 (12.3)	8.0 (11.1)
Mortgages & Loans	4.7(23.8)	5.7(23.7)	5.0 (16.8)	5.4 (17.2)	9.5 (16.7)	15.6 (21.7)
Cash & Bills	8.1(40.5)	8.8(36.6)	12.4 (42.0)	9.6 (30.5)	19.4 (43.1)	30.0 (36.0)
Miscellaneous	0.6 (3.1)	0.9 (3.8)	1.4 (4.7)	3.4 (10.7)	5.7 (10.7)	6.9 (9.7)
Total	19(100.0)	24(100.0)	29.7(100.0)	31.4(100.0)	56.9(100.0)	71.9(100.0)

Source: CBN Review 1980,p.3

premiums fairly regularly throughout the working year. Premium rates are calculated with the assistance of mortality tables,[16] the premium payable to the life office by a particular life assured remaining at a level amount with the passage of time, despite the increasing death risk involved as the life assured matures physically. This ensures that only a portion of the premiums received by the office are expended in claims costs, a reserve fund being created from the remaining portion of premiums, which are available for capital market investment. Since the liabilities of life offices are mainly long term in nature, life offices are interested in minimizing purchasing power risk, and since higher yields on invested funds can be achieved by investing in long term securities, one would expect that the greater proportion of life office funds to be invested in these kinds of assets.

Nigerian life offices did not, during the 1969-1974 period review keep fully invested in long term assets. They invested on average, 37% of their funds in cash and other liquid assets, 23% in government securities, and 13% in stocks, shares and bonds. Comparing this with the situation in the U.K, only 1% of total life funds were held in cash and short term assets in 1963 and 1969, while in the U.S.A, as at the end of 1970, if a policyholder had held the equivalent of a $1000 share in all life companies' assets he would have the following portfolio: $427 in corporate securities consisting of corporate bonds and stocks; $359 in mortgages; $78 in policyholders loans, $53 in government securities,...,$44 in miscellaneous assets, $30 in real estate, and $9 (0.9%) in cash.[17]

The behaviour of the Nigerian life offices has been explained to a certain extent by the nature of the legislation affecting their investment policies and practices.[18] The available data appears to indicate that the life offices did not strictly comply with all of these provisions. Although from 1971 to 1973, the companies complied with the provisions of the law as to a minimum investment of 25% in government securities, in 1969, 1970, and 1974, this was not the case (table 6.9) The figures also indicate that for the three years 1969 through 1971 the percentage invested in real estate was significantly lower than the 10% ceiling stipulated by law. The offices reduced or increased their percentage investment in the various assets according to the underlying yields and it appeared that they were trying to invest in the most profitable assets available to them in the capital market. During this period, the yields on

16. Life assurance rate calculations also involve estimates of future interest rates, expenses and lapse ratios.

17. Life Insurance Fact Book 1971.

government securities were not high and holding assets in mortgage loans and cash appeared to yield higher returns than the other available capital market instruments (see appendix A tables A1-A3). The investment income of all the companies in the market during the period 1960-1973 is displayed in table 6.10(b). The foreign and joint Nigerian/foreign owned offices in life market consistently performed better than the indigenous offices. Although the number of wholly owned foreign companies had gone down to three in 1974, these three contributed about 20% of total life office investments income, while the 16 indigenous companies contributed 24% of the total (table 6.10(b)).

Table 6.10(a)
Nigerian Insurance Companies Net Investment Income 1960-1973 (₦'Million)

Year	Total	Life	%	Non-Life	%
1960	88	4	(4.6)	84	(94.5)
1961	128	10	(7.8)	118	(92.2)
1962	88	20	(22.7)	68	(77.2)
1963	256	180	(70.3)	76	(29.7)
1964	334	276	(82.6)	58	(17.4)
1965	676	386	(57.1)	290	(42.9)
1966	918	532	(57.9)	386	(42.0)
1967	1022	660	(64.6)	362	(35.4)
1968	844	720	(85.3)	124	(14.7)
1969	1030	902	(87.6)	128	(12.4)
1970	1446	1208	(83.5)	238	(16.5)
1971	1692	1404	(83.0)	288	(17.0)
1972	1914	1492	(77.9)	422	(22.1)
1973	2786	2389	(85.8)	397	(14.2)

Source: Life and Non-life investment income data from Nwankwo 1980,p118.

6.2 Regulation and Life Industry Structure and Behaviour 1977-1988

6.2.1 Location of Principal Offices

During this period there was a redistribution of principal offices, with slightly more offices located outside Lagos. This trend was probably a reflection of the increasing economic, and infrastructural developments in the country. Compared with 1971 figures, 29% more principal offices were situated outside Lagos (table 6.11).

18. Section 5(2). For analyses of the investment pattern of Nigerian insurers see, for example, Ogunshola 1976; Akintola-Bello 1983 and Okwor 1986 among others.

le 6.10(b)
tribution of Life Offices Investment Income by Ownership
9-1974

pany	1969 No (%)	1970 No (%)	1971 No (%)	1972 No (%)	1973 No (%)	1974 No (%)
erian	2 (14.3)	6 (9.6)	5 (6.5)	8 (2.9)	10 (4.2)	16 (24.4)
nt	2 (14.3)	2 (10.1)	2 (13.0)	9 (57.6)	10 (55.0)	10 (55.2)
eign	10 (71.4)	9 (84.3)	8 (80.5)	5 (39.5)	6 (48.5)	3 (20.3)
Total	14(100.0)	17(100.0)	15(100.0)	22(100.0)	26(100.0)	29(100.0)

Source: As in Table 6.9

Table 6.11
Location of Nigerian Life Insurance Companies Principal Offices
1980-1987

Class of Bz	1980 Lagos	Other	Total	1982 Lagos	Other	Total	1987 Lagos	Other	Total
Life	3 (13.6)	-	3 (13.6)	3 (11.5)	-	3 (11.5)	2 (6.7)	1 (3.3)	3 (10.0)
Composite	13 (59.1)	6 (27.3)	19 (86.4)	15 (57.7)	8 (30.8)	23 (88.5)	16 (53.3)	11 (36.7)	27 (90.0)
Total	16 (72.7)	6 (27.3)	22(100.0)	18 (69.2)	8 (30.8)	26(100.0)	18 (60.0)	12 (40.0)	30(100.0)

In 1982 these offices were mainly located in state capitals in the western and eastern parts of the country, and in 1985, two companies were headquartered in the north, specifically in Kaduna, a city that was becoming a commercial centre (table 6.12). However, up till 1988. only one of the top ten companies (The Universal Insurance Co.) was principally located outside Lagos.

Table 6.12
Life Company Principal Offices Located Outside Lagos 1982-1987

Company	Location	Ranking by Market Share 1982	1985	1987
Trans Nig	Ibadan	-	17	23
Worldwide	Ibadan	-	26	26
Palm Beach	Enugu	21	23	28
Universal	Enugu	10	10	9
Bendel	Benin	7	12	11
Rivbank	Port-Harcourt	17	11	14
Gateway	Ilorin	16	19	20
Manilla	Calabar	13	-	16
Towergate	Abeokuta	-	-	29
Foundation	Owerri	-	-	-
Leadway	Kaduna	-	-	19
First Nig	Kaduna	-	-	27
Confidence	Akure	-	-	21
Hallmark	Owerri	-	-	-

6.2.2 Number and Size Distribution of Life Offices

Following the pattern in the previous period, the number of pure life offices in the market decreased between 1977-1987. There was a slight increase in the number of composites, from 17 in 1975 to 26 in 1986 (table 6.13). The size distribution of the life offices between 1980 and 1987 appears to indicate the increasing dominance of larger size life offices (that is, offices with premium incomes in excess of ₦10 million) operating in the market with an increase in the number of smaller firms operating on the fringe of the market (table 6.14).

There was a slight decrease in market share of about 2% between 1985-1987. Small size firms have been defined as those offices with life premiums less than ₦10 million. The data indicates a slight increase in the number of "small" life offices between 1980 and 1987 (an increase of three offices).

Table 6.13
Registered Insurance Companies in Nigeria
1975-1987

Class of Bz/Year	1975	1976	1977	1978	1980	1981	1982	1983	1984	1985	1986	1987
Life	9	6	6	6	4	4	3	3	4	4	4	3
Non-Life	43	37	38	42	55	55	63	63	65	67	69	78
Composite	17	16	15	15	21	21	23	24	25	25	26	30
Total	69	59	59	63	80	88	90	94	96	93	96	111
Life & Composite	26	22	21	21	25	25	26	27	29	29	30	33
Returns	n/a	n/a	n/a	20	20	21	23	27	26	27	28	31

Table 6.14
Size Distribution of Nigerian Life Offices
1980-1987 (₦'Million)

Size	1980			1982			1985			1987		
	No	Value	M/S	No.	Value	M/S	No.	Value	M/S	No.	Value	M/S
Below 1	7	1.8	1.9	8	2.2	1.8	12	4.8	2.9	13	7.0	3.5
1-4.99	6	14.2	14.8	7	15.8	12.9	17	18.8	11.2	8	17.6	7.8
5-9.99	6	41.4	43.2	3	19.8	16.1	2	13.0	7.7	1	5.2	2.6
10-14.99	2	21.6	22.5	5	61.7	50.3	1	11.0	6.6	2	24.0	2.0
15-19.99	1	16.9	17.6	-	-	-	3	48.4	29.0	3	51.8	25.8
20 & over	-	-	-	1	23.1	18.9	2	71.3	42.6	3	96.9	48.3
Total	22	95.9	100.0	24	122.7	100.0	27	167.3	100.0	30	202.5	100.0
Below ₦10	19	57.4	59.9	18	37.8	30.8	31	36.6	21.8	22	29.8	13.9
Above ₦10	3	38.5	40.1	6	84.8	69.2	6	130.7	78.2	8	172.7	76.1
ASF		4.33			3.86			1.8			2.25	

Their combined market shares did not increase in a corresponding manner, but actually fell from about 60% to 14% in the same period. Asset values also fell from about ₦57 million to ₦38 million, that is by around 33%. Conversely, for the larger sized firms, the total number of offices rose from three to eight in the same period, while market shares increased considerably by almost 100%, from about 40% (1980) to 76% (1987). Total industry assets owned by this category of life offices also increased considerably from ₦38.5 million in 1980 to ₦172.7 in 1987, an increase of over 300%. The trend appears to be towards an increasing degree of market power in the life industry, firms with life premiums in excess of ₦10 million having a monopoly of life industry premium income and assets.

6.2.3 Ownership Structure and Size of Firm

During this period the number of national (that is companies with government equity) increased. The joint Nigerian/foreign venture companies constituted about one third of the market. None of the indigenous companies was among the top ten offices in the market while on average in 1982, 1985 and 1987, the national companies underwrote a third of life premiums. For the three years, joint venture insurers wrote over half the total premiums, with the government/foreign companies having the greatest market shares (table 6.15). During this period, two large offices with joint foreign and government ownership (the British American Ins. Co. and The Crusader Ins. Co.) obtained indigenous equity participation in their companies. Further analysis of ownership structures among the other offices not included in the top ten list reveals that most of them were indigenous companies while a smaller percentage were owned by the federal and state governments. The dominance of foreign companies in the 1960-1976 period had been replaced by the dominance of national and joint venture companies.

The average size of firm (measured by gross premiums) fell from ₦4.33 million in 1980 to ₦2.25 million in 1987. The sharpest drop was in 1985, where the average size fell to ₦1.8million[19]. A rough estimate of the optimum size of firm (the size of firm that contributes increasing amounts of premium income over the years) appears to be

19. The median has been used as the measure of the average size of firm because of the skewness of the distribution. It is given as:

$L+jw/f$, where

L = Lower true limit of the class in which the median is located,

₦15 million and above. This implies that majority of the life offices operating in the market are not doing so at optimum efficiency, with the offices operating "optimally" contributing about 17% of the total market premium in 1980, 19% (1982), and over 70% in 1985 and 1987.

Table 6.15
Ownership Structure of Top Ten Life Offices in Nigeria 1982-1987

Ownership	1982		1985		1987	
	Number	M/S	Number	M/S	Number	M/S
Ind	-	-	-	-	-	-
Nat	5	31.0	4	33.2	4	34.5
Nat/For	3	40.5	2	24.9	3	33.9
Nat/Ind	-	-	-	-	-	-
For/Ind	-	16.8	2	14.9	2	14.3
For/Nat/Ind	2	-	2	18.6	1	7.7
Total	10	88.3	10	91.6	10	90.4

Table 6.16(a)
Nigerian Life Office Concentration Ratios by GPI 1978-1988

CR	1	3	5	10
1978	17.6	48.9	66.0	90.9
1980	17.6	40.1	58.2	87.8
1981	18.2	40.9	61.2	92.7
1982	18.8	41.2	60.9	88.3
1983	29.5	52.1	70.8	90.7
1985	17.9	45.1	67.6	90.2
1986	30.2	52.9	70.6	93.4
1987	22.8	47.9	65.8	90.3
1988	18.1	44.1	64.4	89.9

j = is the number of values still needed to reach the median after the lower limit of the class containing the median has been reached

f = the frequency of the class interval containing the median and

w = the width of the class interval.

6.2.4 Concentration

Concentration gives an indication of the degree of market power present in an industry. Decreasing levels of concentration in the life assurance market could be an indication of market growth, that is, an expanding life industry[20] and an intensification of competition.

Figure 6A

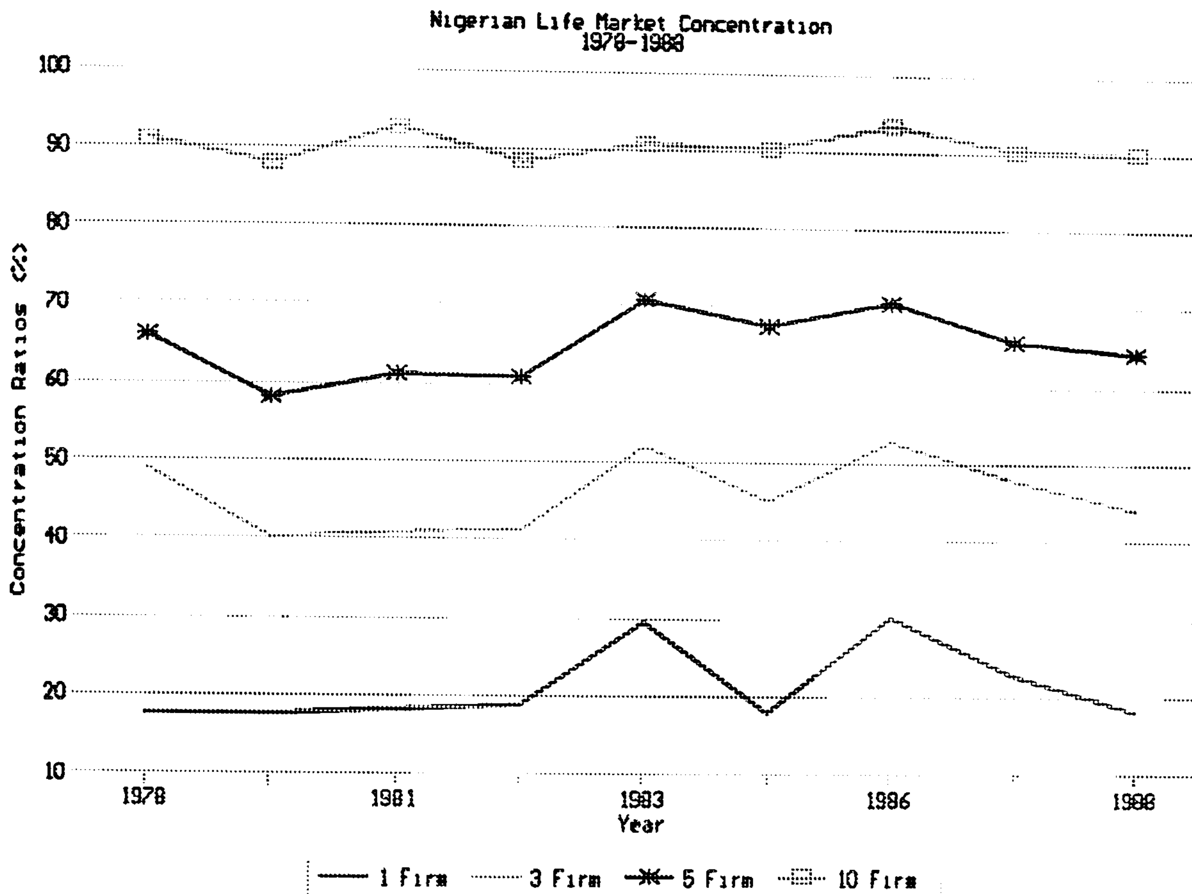

Table 6.16(b)
Nigerian Life Office Concentration Ratios by Total Assets 1982-1987

CR	1	3	4	5	10
1982	21.7	44.3	51.4	57.1	79.8
1985	41.8	57.4	63.7	68.1	83.6
1987	49.7	58.5	63.8	67.5	80.0

20. See Cummins et Al 1972.

Concentration has been measured as the percentage of total life industry premiums which is contributed by the largest firms. For the period 1980 to 1985, the insurance market in general and life market in particular was highly concentrated. It appears from 1987 figures that there is a decrease in concentration over the previous years, but future data will have to be examined to see whether this trend will continue.

Table 6.16(c)
Nigerian Insurance Market Concentration Ratios
1984-1987

CR	1	3	4	5	10
1984	20.5	35.6	40.9	45.4	59.7
1985	22.2	40.3	46.1	50.9	65.3
1986	24.5	41.0	46.2	51.6	78.6
1987	37.3	50.7	55.1	59.0	71.0

Note: CR denotes concentration ratio

Table 6.17(a)
Entry into the Nigerian Life Market
1980-1988

Year	Total	Entry		Exit	
	Entry	L	C	L	C
1980-1982	+1	0	+2	-1	0
1982-1985	+4	+1	+4	-1	0
1985-1988	+4	0	+5	-1	0
1980-1988	+9	+1	+11	-3	0

6.2.5 Turnover/Entry

Turnover, that is, a change in the size ranking of the larger firms in a given market (Koch 1974,p.166) is said to be an indicator of dynamic competition. The rapidity of turnover is indicative of a competitive struggle for position (Scherer 1980,pp.73-74), while a decreasing turnover rate would result from the development of more effective bars to entry or "Trustified Capitalism" (Schumpeter 1939,p.149).

Although the concentration ratios indicate the exercise of some monopoly power by the largest life offices, there is evidence of a competitive struggle for market shares among them. If 1980 is taken as the base year, it can be seen from table 6.17(b) that the market share ranking of these life offices has, with the exception of 1981, been changing.

Table 6.17(b)
Turnover Among the Top Ten Nigerian Life Offices
1980-1987

Company/Year	1978 M/S (R)	1980 M/S (R)	1981 M/S (R)	1982 M/S (R)	1983 M/S (R)	1985 M/S (R)	1986 M/S (R)	1987 M/S (R)	1988 M/S(R)
Great Nigeria	16.5 (2)	17.6(1)	18.2 (1)	18.8 (1)	12.6 (2)	15.1 (2)	13.1 (2)	14.3 (2)	14.9 (2)
Brit/American	17.6 (1)	12.0(2)	11.4 (2)	10.6 (4)	9.2 (5)	11.1 (5)	8.8 (5)	8.7 (5)	9.9 (5)
Crusader	9.7 (4)	10.5(3)	11.3 (3)	9.1 (5)	9.5 (4)	11.4 (4)	8.6 (6)	7.7 (6)	8.3 (7)
American Int	14.8 (3)	9.6(4)	10.5 (4)	11.3 (2)	29.5 (1)	17.9 (1)	30.2 (1)	22.8 (1)	18.1 (1)
African Alliance	7.6 (6)	8.5(5)	9.2 (6)	11.1 (3)	10.0 (3)	12.1 (3)	9.6 (3)	9.2 (4)	10.4 (4)
NICON	7.4 (5)	7.1(6)	9.8 (5)	8.2 (6)	6.6 (6)	6.5 (6)	8.9 (4)	10.8 (3)	11.1 (3)
Niger	3.9 (9)	6.7(7)	8.3 (7)	4.2 (9)	2.9 (9)	3.6 (9)	5.1 (8)	6.8 (7)	8.3 (6)
Nigerian General	2.0(11)	5.9(8)	0.9(12)	1.3(15)	0.4(13)	1.4(12)	1.3(11)	1.0(13)	1.1(11)
Royal Exchange	6.8 (7)	5.4(9)	6.4 (8)	5.7 (8)	4.6 (7)	5.5 (7)	5.0 (7)	5.0 (8)	4.8 (8)
United Nig. Life	4.5 (8)	4.5(10)	3.9 (9)	2.9(11)	3.1 (8)	3.7 (8)	n/a*	2.4(10)	2.5 (9)
Universal	1.1(14)	3.0(11)	3.7(10)	3.1(10)	2.7(10)	3.3(10)	2.8 (9)	2.6 (9)	n/a*
Bendel	2.1(10)	2.6(12)	1.7(11)	6.2 (7)	1.3(12)	1.6(11)	1.3(10)	1.4(11)	1.6(10)

* Life premium figures unavailable

Table 6.17(c)
Entrants into the Nigerian Life Market
1980-1988

Life Office	1988 Premium	Type	Ownership
Worldwide	₦377,807	C	Nat
Hallmark	n/a	C	Ind
First Nigeria	₦731,969	L	Ind
Towergate	₦122,650	C	Nat/Ind
Amicable	₦626,320	C	Ind
Foundation	n/a	C	Ind
Nigeria French	n/a	C	For/Ind
Confidence	n/a	C	Nat
British American*	₦20,891,694	C	For/Nat
African Prudential*	₦471,460	C	Ind
Leadway*	₦2,055,326	C	Ind

Notes: (1) Nat, Ind and For denote National, Indigenous and Foreign ownership respectively (2) * denotes cross entrant (3) n/a, premium data for 1988 unavailable.

Monopoly power cannot exist in the long run except where it is supported and protected by barriers to entry.[21] Between 1980 and 1988, 12 life companies (11 composite and one specialist) entered into the market while three life companies exited from the market. Total entry during the period was one company a year while the exit rate was 0.33 (table 6.17(a)). Three of the new entrants (the British American, Leadway and the African Prudential, specialist life companies) were cross entrants[22] into the market. None of the new entrants (excluding one cross entrant, the British American) was ranked among the top ten companies in the market, and only one specialist company, First Nigeria, commenced business (table 6.17(c)).

It appears, so far, that different types of entrant will suffer different degrees of disadvantage, with entrants from closely related markets being less disadvantaged than those from other markets.[23] The rates of entry/exit as well as the low level of turnover experienced during the period seem to suggest the existence of significant entry barriers.

21. A barrier to entry may be any advantage held by existing firms over those firms that might potentially produce in a given market (Bain 1965). Entry is defined as the production of new output in a given market which may emanate from an already existing or new firm. Stigler however argues that the act of entry itself consists only of the entry of new firms previously not in the market.

22. A cross entrant is a firm already involved in underwriting insurance at the date of entry, whether directly underwriting classes of business other than life insurance business, or established as a subsidiary of a group of companies already established in the insurance market (Franklin and Woodhead 1980).

The low entry rates and high concentration levels suggest that (1) entry into the market is difficult, probably because of result of the technological barriers in the form of the expertise required in this market and (2) the industry is oligopolistic, with the largest firms having the monopoly of industry premiums and assets. However, there is evidence of some competition among the larger offices. The slight decrease in 1987 concentration levels may be indicative of a future tendency towards increasing competition in the industry, but no definite conclusions can be drawn.

6.2.6 Growth

Since 1982, the growth of real life premiums has been declining, although it has remained the most significant contributor to total market premiums since 1983 (tables 6.18, 6.19 & figure 6B). However, the emergence of life insurance as a significant contributor to total market premiums is not necessarily because of an increase in life assurance consumption, but as a result of decreases in the volume of motor premiums in the non-life market. Motor vehicle insurance has traditionally been a very important sector of insurance business in Nigeria. In fact, the first legislative instruments governing insurance business in the country were the motor vehicle ordinances. During the oil boom era the growth of this market was aided by the large scale importation of motor vehicles and the generous car loans and allowances paid to workers. The subsequent decline in motor premium income has been attributed to various factors such as the drastic cutback in the domestic assembly and production of motor vehicles, the withdrawal of car loans and allowances to workers in the period 1978-1979, and the inability of many insureds, who unable to pay high premiums for comprehensive cover, have changed to 3rd party cover, thus lowering the total motor premiums to the market.[24] Although the average growth rate of the life market during this period was 17%, in real terms this amounted to 3.4% in real terms, a considerable decline over the previous period.

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23. See Franklin and Woodhead 1980, chapter three for a detailed discussion.

24. The Nigerian Insurance Yearbook 1987,pp.165-166.

Table 6.18
Percentage Distribution of Various Classes of Insurance Business 1977-1987

Rank/Year	1977	1978	1979	1980	1981	1982
1	M (35.7)	M (30.6)	M (28.8)	M (24.0)	G (25.0)	M (24.2)
2	A (22.1)	A (22.1)	G (19.4)	G (19.4)	M (23.6)	G (22.0)
3	G (17.9)	G (17.9)	L (18.7)	L (21.0)	L (21.2)	L (20.1)
4	L (17.6)	L (17.6)	A (18.0)	A (18.6)	A (17.9)	A (19.2)
5	F (11.8)	F (11.8)	F (15.1)	F (12.9)	F (14.5)	F (14.5)

Rank/Year	1983	1984	1985	1986	1987
1	L (24.4)	L (25.9)	L (27.3)	L (26.8)	A (28.8)
2	M (23.5)	G (22.4)	G (20.8)	F (20.3)	L (20.6)
3	G (23.1)	M (22.2)	M (20.5)	A (18.0)	F (20.2)
4	F (16.5)	F (17.6)	F (17.3)	M (17.9)	M (15.4)
5	A (12.5)	A (11.9)	A (12.1)	A (17.0)	G (15.0)

Notes: (1) L, M, F, G and A denote life , motor, fire, general and marine and aviation business respectively (2) Figures based on gross premium income.

Figure 6B

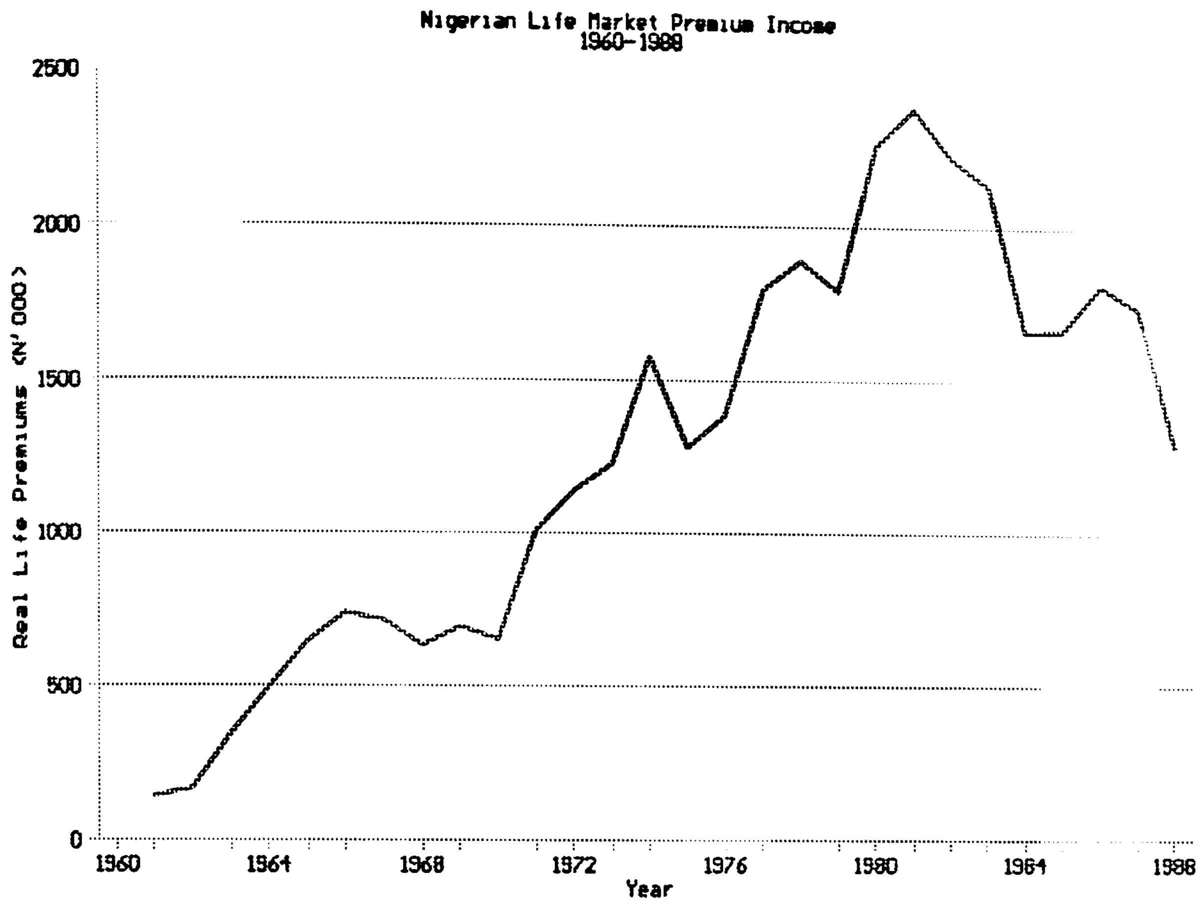


Table 6.19
Nigerian Life Office Gross Premium Income 1976-1988(N'000)

Year	Life Premium Nominal	Life Premium Real	Growth (%) Nominal	Growth (%) Real
		1985=100		
1976	34490	1386	-	
1977	50899	1797	47.6	29.6
1978	65250	1892	28.2	5.3
1979	69102	1794	5.9	-5.2
1980	95886	2264	38.8	26.1
1981	121869	2382	27.1	5.2
1982	122768	2228	0.7	-6.5
1983	145023	2136	18.1	-4.1
1984	157871	1666	8.9	-22.0
1985	167297	1672	5.9	0.4
1986	191262	1816	14.3	8.6
1987	202640	1745	5.9	-3.9
1988	207877	1295	2.6	-25.8

6.2.7 Investment Behaviour

The investment pattern of the life offices remained, on the whole, the same as in the post-colonial period. The highest proportion of investment funds remained in government securities, and during this period, the minimum investment has been about 20% , with an average of about 24%. The life offices, according to the available data have not kept fully invested in the government securities as required by law for the 1979-1983 and 1985 period. They have however been increasing their total investment in corporate securities (and policy and other loans to a lesser extent) while decreasing, on average, their investment in real estate, and mortgage loans. As with the 1960's, an inordinately high proportion of funds has been kept in cash and other short term assets.

A comparison of the yield rates on the various financial instruments explains the life offices investment pattern. The most profitable instruments are corporate securities, the yields on government stock and interest rates on bank deposits being comparatively lower. The returns on government financial instruments and bank deposits in this period did not keep up with the inflation rates in the country (appendix A table A4).

6.2.8 Life Insurance Intermediaries

During this period, the distribution method for life assurance products remained the same as in the earlier period. Life insurance products were marketed by life (full-time and part-time) insurance agents, as well as insurance brokers.[25] The number of registered brokers in the market at this time increased significantly over the 1974 figure. About 90% were wholly owned by Nigerians, the percentage of joint indigenous/foreign business having deceased over the period from 19.6% (1978) to 11% (1987) (table 6.20). As far as the public perception of their services was concerned, there appeared to be no improvement in this area. The agents and brokers were still failing to remit premiums collected from policyholders to the insurance companies,[26] and it appeared that the Insurance Department was unable to discipline erring intermediaries. The insurers alleged that the intermediaries were investing the outstanding premiums in short term bonds in order to earn some money on the funds

25. The Nigerian Insurance Year Book 1979, pp.187-189.

before remitting them to the insurance companies at their convenience. In January 1987, the Director of Insurance issued a circular which stated measures the Department was taking to control the situation. Brokers and agents licenses would not be renewed unless they presented evidence of the payment of all outstanding premiums to the insurance companies.[27]

Table 6.20
Registered Life Brokers in Nigeria
1976-1987

Type/Year	1976	1978	1980	1982	1984	1986	1987
Life	2	2	2	3	3	3	2
Life&General	30	44	52	67	78	94	99
Total	32	46	54	70	81	97	101

Compiled from data in various issues of the Nigeria Insurance Yearbook

However, the companies were being subjected to a subtle form of blackmail. Some insurers were reluctant to report erring brokers to the Insurance Department as the broker would blacklist the company in future,[28] and the company might not recover it's outstanding premiums. In addition to this some intermediaries were demanding what they referred to as "acquisition costs", which was in effect an inducement given to brokers to encourage them to place business with the insurer.[29] Since the life market was competitive, companies had no option but to pay up.

The problem of supervision also extended to the insurers. Despite the strict licensing requirements in the 1976 Decree, some unlicensed companies still managed to operate in various parts of the country.[30] In addition to this insurers were not submitting adequate returns to the Insurance Department and the Central Bank as required by law.[31] The public perception of insurers did not improve in this period. Poor after

26. The Director of Insurance remarked on this unhealthy practice in an address he gave at a forum arranged by the Nigerian Corporation of Insurance Brokers on "The Broker and the Insurance Industry" (WAICA Journal 1987, Vol.XI p.153). Discussions with industry executives confirmed the Directors comments.

27. Ibid, p.153 and also The Business Concord, Tuesday September 23 1987,p.16.

28. One small sized insurer in the market stated that they had to put up with the brokers behaviour because they could not afford to be "too choosy" since they needed all the business they could get (The Business Concord, Ibid). An executive in one of the large national companies interviewed between May-July 1991 confirmed that the company had to put up with a lot of unethical behaviour from the intermediaries for the same reasons.

29. Ibid,p.153.

sales service, which in many cases resulted in disputes over insurers liability to policyholders contributed to the consumers dissatisfaction with the insurers.[32]

6.2.9 Life Insurance Products/Prices

During this period, group life insurance dominated the sales portfolios of life insurance companies, and the amount of industrial life insurance underwritten was insignificant. Endowment insurance policies in ordinary life accounted for 76% of the number and 79% of the value of ordinary life insurance in force in 1987. Between 1979 and 1987 the average proportions of the various kinds of business underwritten were as follows: group life: 73.3%, endowment 23.0%, term 3.4% and whole life insurance 0.3%. There was a predominance of participating policies and most of the without profit policies were mortgage protection and other temporary assurances.

The level of life insurance consumption was still quite low. Although the number of individual life policies increased from 96,082 in 1979 to 222,592 in 1987, in terms of the value of policies there was a decrease of almost 200% over 1979 values. The value of group life insurances in force however, increased by about 200% between 1979 and 1987.[33]

During this period there was very little innovative activity in the industry.[34] The basic products offered in the individual life market were the whole life, endowment and term insurances. Research and development activities were practically non-existent in the companies.[35] Although one of the functions of the Nigeria Reinsurance Corporation was to conduct research into the industry, the available evidence suggested that it was not initiating any serious projects. The main study it had undertaken during the period was an outdated manpower development study of the

30. The Business Concord, Friday October 23 1987,p.1.

31. The Deputy Governor of the Central bank of Nigeria commented upon this in The Bullion, Vol.15 (2) April/June 1991, p.4.

32. The Minister of Finance and Economic Development Dr. Chu Okongwu commented on the industry's "...poor image..." at a symposium organised by the Nigeria Reinsurance Corporation in Lagos (The Guardian, Tuesday January 26, 1988,p14). See also, The Democrat, Thursday August 11, 1988,p10).

33. Figures have been obtained from The Nigeria Insurance Digest 1989, pp.59-64.

34. This lack of innovative activity was also the subject of the Minister of Finance and Economic Development's comments (The Guardian, ibid).

industry which was basically a headcount of the employees in the insurance sector. Very little attention had been paid to the life market despite the fact that the consumption of insurance services in this sector was very low.[36]

In the mid 1980's however, in an effort to increase the consumption of individual insurances, some of the bigger life companies (for example, the American International Ins. Co., Great Nigeria and Crusader) began to offer new[37] life insurance products such as the Multi-Plan, Tree Payment or Optional Endowment policy.[38] Additionally, some of these companies also began to market unit or investment linked policies. The banking sector appeared to take advantage of the lack of innovative activity in the life market to introduce schemes which provided certain types of "free" insurance cover for their customers who held certain kinds of bank accounts. Although the banks marketed the schemes,[39] various insurance companies underwrote them. The incursion of the banks into this area was in general not received kindly by the insurers.[40]

Insurance rates in the life market were believed to be high.[41] The insurers defended these rates on the basis that they take into consideration the expected mortality experience as well as expenses and future interest rates. Thus, increasing inflation in the economy, the variability of the company income tax chargeable as well as the Government's policy of discriminatory taxation of insurers pension funds[42] are factors upon which life insurers base their justification for these rates. Additionally, although life rates are not directly regulated by the Insurance Department, in accordance with regulatory rules, all proposed new policies had to be submitted to the Director of

35. The Business Times, Monday July 23 1990,p.10.

36. This conclusion has been arrived at on the basis of information obtained from the Research and Development Department of the Nigeria Reinsurance Corporation in June 1991.

37. These products were new to the Nigerian life market.

38. The policy offers partial maturity payments based on a percentage of the sum assured to the policyholder at agreed intervals during the duration of the policy. The rates of return on such policies are supposed to be high and the policyholder has the option of reinvesting the partial maturity proceeds.

39. The Universal Trust Bank (UTB) and the United Bank of Africa (UBA), two of the largest banks in the banking sector market these policies.

40. See the Business Concord, Tuesday June 5 1990.

41. This information was obtained from life insurers in the market and not, as would be supposed, life insurance consumers.

42. See section 5.2211.

Insurance for approval before they were placed on the market. The approval process took months, sometimes years, by which time market conditions in the volatile Nigerian economy could have changed to such an extent as to render the original rates uneconomical. There were no official guide-lines for the rate approval process and the rates proposed by the insurers were simply rubber-stamped by the Director of Insurance.[43] Some insurers were of the opinion that the unnecessary delay in the approval of new policy forms and rates has contributed to the lack of new product development in the industry.

6.3 The Economic Significance of the Nigerian Life Market

The governments regulatory objectives have, among other things, been focused on increasing the social and economic significance of the Nigerian life insurance market. A measure of the social significance of the market is the increased consumption of life insurance services.

Table 6.21
Nigerian Life Premium Income as a Percentage of Personal Disposable Income 1975-1985

Year	Premiums	PDI	LPI/PDI%	PS/PDI%
1975/76	25689	18284	0.14	26.20
1976/77	34490	23266	0.15	31.40
1977/78	50899	26197	0.19	31.05
1978/79	65250	29404	0.22	17.23
1979/80	69102	36419	0.19	28.81
1980	95886	43199	0.22	26.63
1981	121869	44874	0.27	17.93
1982	122768	45398	0.27	14.56
1983	145023	48170	0.30	14.37
1984	157871	52817	0.29	16.29
1985	167297	58760	0.29	15.34

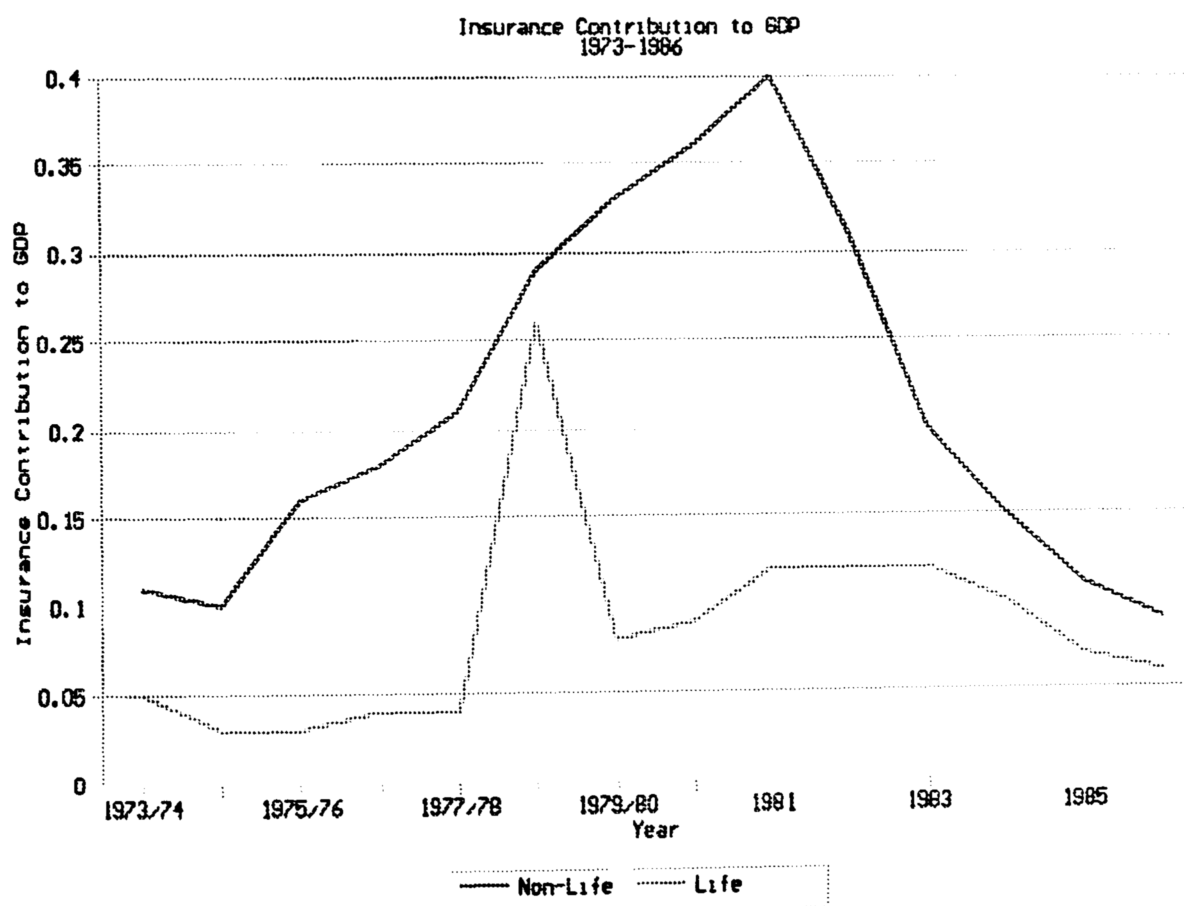
Source: Compiled from the following, (1) Life Premium figures in ₦'000 from Nigeria Insurance Yearbook 1987, (2) PDI and savings figures in ₦'million, Annual Abstract of Statistics, Lagos various issues

Findings in various studies[44] have established that the demand for life insurance increases more than proportionately with increases in income. A comparison of the growth trends in Personal Disposable Income (PDI) with the growth in life premiums

43. This state of affairs is not surprising since there are no professionally qualified actuaries in the Insurance Department to examine the adequacy or otherwise of the proposed rates.

for the 1975-1985 period reveals that there has been a marginal increase of life premiums with increases in PDI (table 6.21). The highest growth in demand for life insurance was recorded in the period between 1980 and 1981, during the oil boom era, when the country was experiencing a period of economic prosperity. Correlation of the two shows that growth in life premiums and personal disposable income are almost perfectly positively correlated with a correlation coefficient of 0.98. Life premiums however, represented an insignificant proportion of institutional saving. Personal income and savings data beyond 1985 were unavailable at the time of the study. The contributions of the life market to GDP measures it's economic significance. This has been marginal, and significantly lower than non-life market contributions. The figure for the life market rose sharply between 1977-1979, and declined just as sharply between 1979 and 1980 (figure 6C). Since 1984, life contributions, like non-life figures, have been on the decrease.

Figure 6C



Although the demand for life insurance services (growth in total life premiums) was positively correlated with the growth in the economy (growth in GDP), the relationship was weak with a correlation coefficient of 0.33.[45] Post 1986 data were

44. See for example, Carter 1972, Diacon 1980 and Franklin and Woodhead 1988.

unavailable at the time of the study. A comparison with the figures for the U.K and U.S.A markets reveals that comparatively speaking, the Nigerian figures are quite low (table 6.22). The contribution of life premiums to GDP in developing countries is generally low. Data for 1984 data indicate that out of 67 countries surveyed, only eight had life premiums/GDP figures greater than 1%.[46]

Table 6.22
A Cross-National Comparison of Life/Non-Life Insurance Expenditure as a Percentage of GDP/GNP 1952-1982

Year	U.K (1)	U.S.A (2)	Nigeria (3)
1952	1.78/2.74	2.84/2.40	n/a
1962	2.11/3.24	3.60/2.61	0.30/0.05
1972	2.64/3.05	4.38/2.58	n/a
1977	2.87/2.79	5.05/2.57	0.21/0.04
1980	2.90/2.98	4.70/2.47	0.36/0.09
1982	2.88/3.46	4.52/2.70	0.40/0.12
1986*	8.0	8.2	1.15

Source: (1) columns (1) and (2) 1952-1982 figures, Diacon 1990,p.19
(2) 1986 figures from Sigma, No.5/May 1988,p.13
Notes:(1)*1986 figures represent total insurance market contributions to GDP (2) U.K and U.S.A figures expressed as a percentage of GNP, Nigerian data as a percentage of GDP

Table 6.23
Life Insurance fund and Reserves Contribution to GDP 1977-1986

	Year ₦'000	Life Funds ₦'million	Life Funds/ GDP %
1977	470,285	32,052	1.47
1978	267,070	33,360	0.80
1979	896,523	39,939	2.24
1980	470,460	43,280	1.09
1981	632,564	43,450	1.46
1982	654,135	60,483	1.08
1983	639,351	63,293	1.01
1984	700,172	69,950	0.89
1985	837,167	78,776	1.05
1986	1,017,521	79,740	1.28

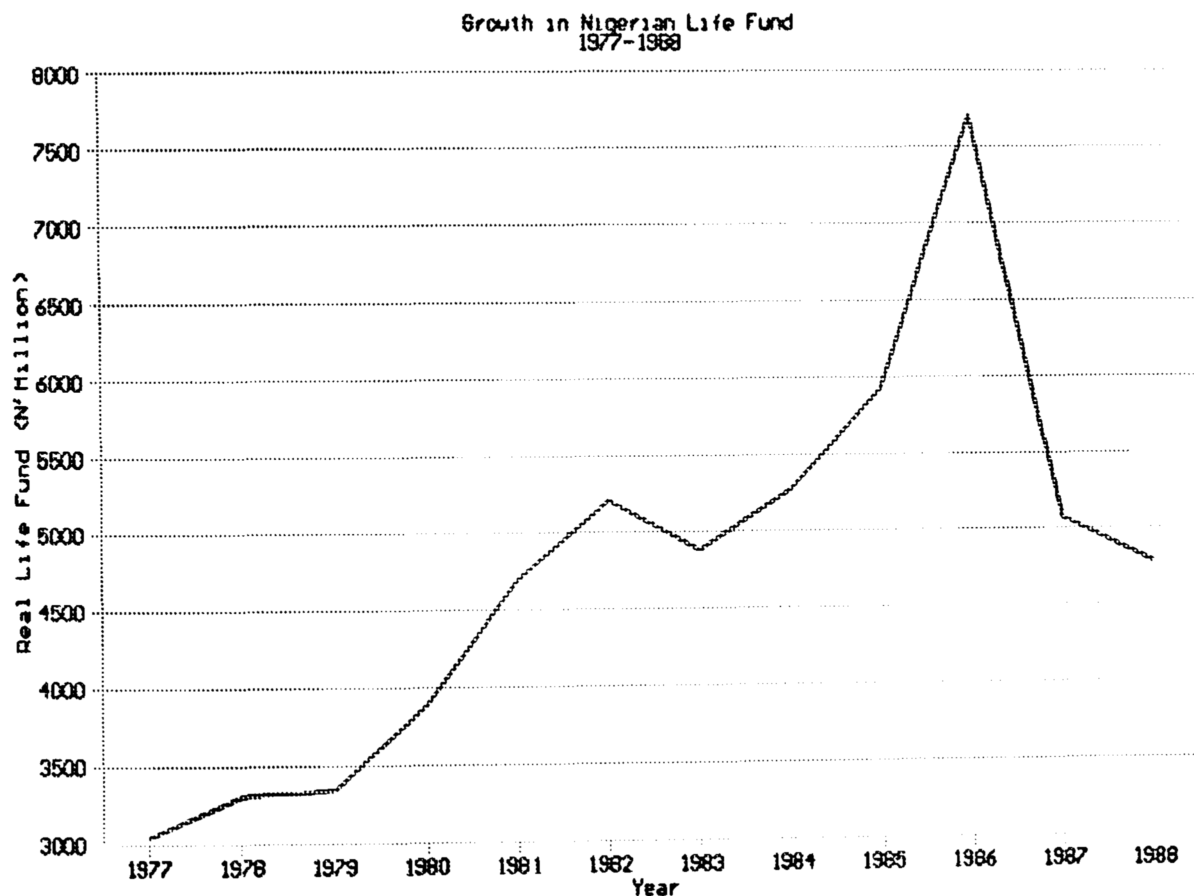
Source: Compiled from premium and life fund data from the Insurance Department, Lagos

45. See appendix B for GDP figures.

46. UNCTAD TD/B/C.3/220,pp.3-14. This was a statistical survey on insurance and reinsurance operations in developing countries carried out in 1984. To date the study has not been updated.

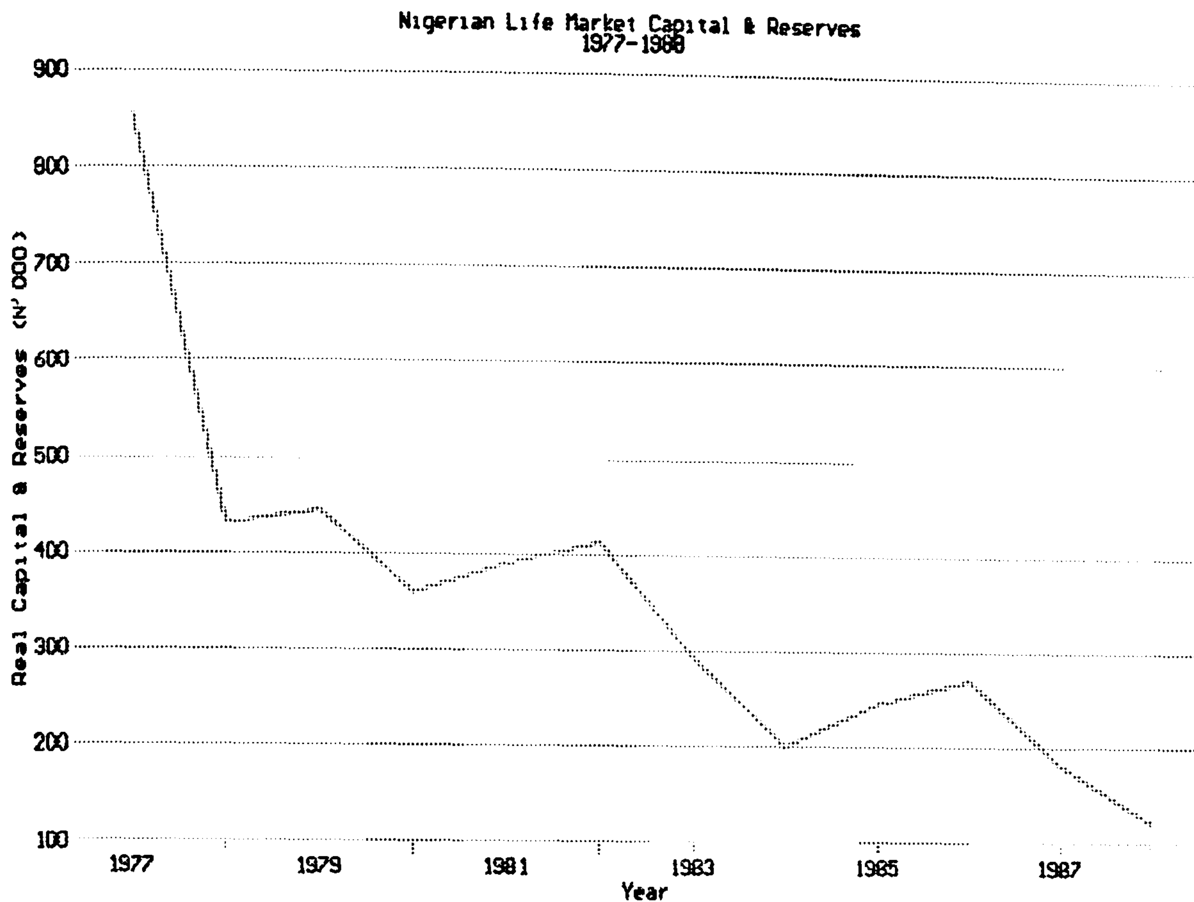
Life office funds and reserves are important to the well-being of policyholders, life offices and the economy as a whole. These funds are set aside to meet the life offices future contractual obligations to policyholders and their adequacy and growth is essential for solvency purposes. Additionally, they are a source of the much needed investment funds in the economy. Although there is insufficient information to estimate individual company solvency, it follows that if the life fund and reserves are growing in real terms, policyholders interests are being protected. There has been little improvement in the economic significance of life funds and reserves over the period from 1977 to 1988. Average real growth rates for the life fund and capital and other reserves were about 6% and -6.8% respectively.

Figure 6D



The size of the total industry life fund in real terms increased between 1977 and 1982, the period of economic prosperity, dropping slightly between 1982 and 1983. However the figure more than doubled, rising to over ₦7,500,000 in 1986, and then started to decline progressively from that time (figure 6D). In order to place these increases in proper perspective, they were estimated as a percentage of total GDP over the period. This showed no significant improvement over the period. In fact the 1986 ratio (1.28%) was less than the 1977 figure (1.47%) (table 6.23). The size of life market capital and contingency reserves actually decreased significantly in real terms over the period (figure 6E).

Figure 6E

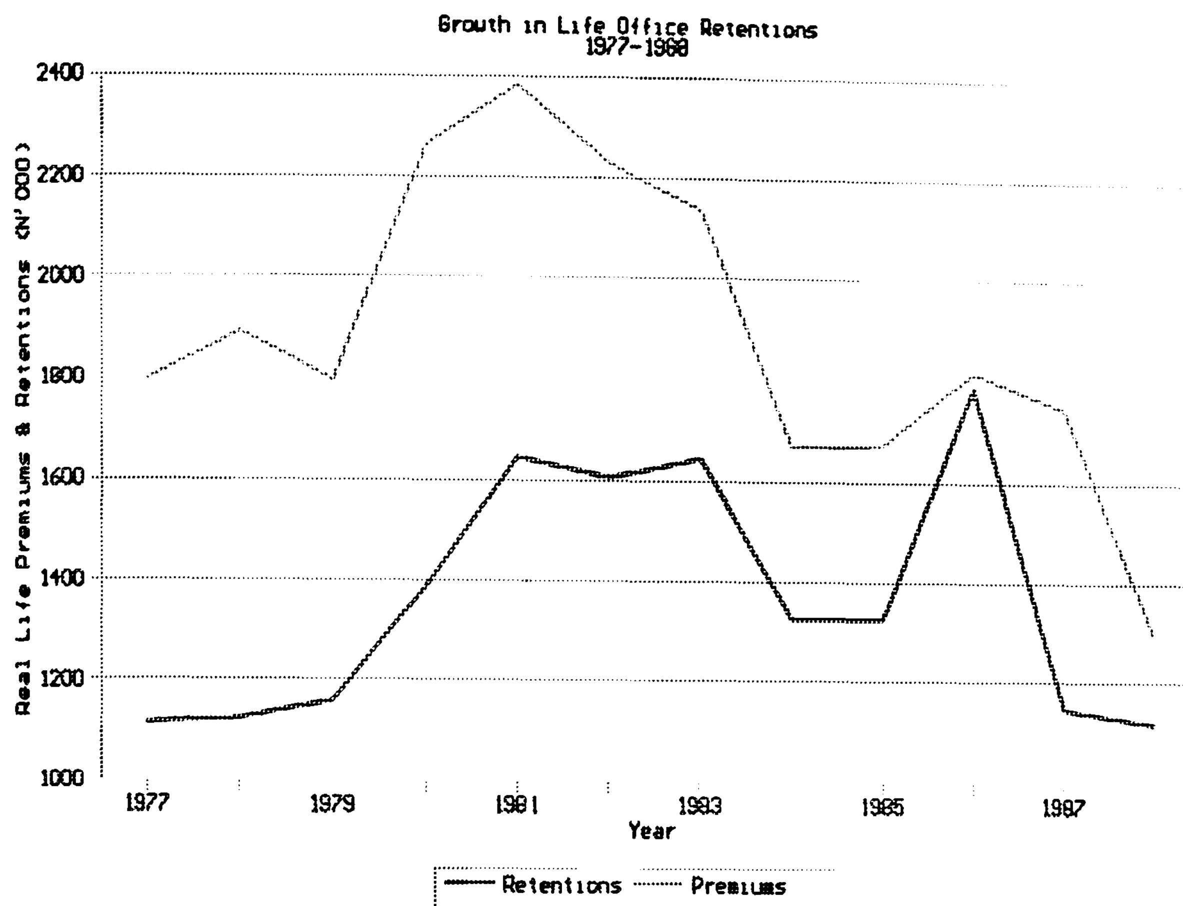


6.3.1 Reinsurance

The primary reason for the establishment of the Nigeria Reinsurance Corporation in 1977 was for the corporation to focus on developing the reinsurance market in Nigeria. One of the ways in which this was to be achieved was through the reduction of the level of market cessions to overseas reinsurers in order to increase the capacity of the domestic market.

Although the average growth rate for retentions for the 1977-1988 period was apparently 15.2%, in real terms this amounted to only 1.74%. The data on life insurer retentions indicates that generally speaking, insurers have been retaining, on average, over 90% of life premiums (table 6.27). The growth pattern of real retentions followed that of real premiums closely, suggesting that over the period the life offices retained more with rises in premium income and vice versa (figure 6F) In 1986, the offices were retaining almost all their premiums.

Figure 6F



During the 1977-1988 period the amount of local cessions exceeded that of international cessions considerably. About ₦65 million worth of life premiums was ceded in the market out of which ₦21 million (about 32%) was accepted locally. The amount of direct international cessions to overseas (European) markets was about 6% of total cessions. Thus about 62% of the total market cessions were made to the Nigeria Reinsurance Corporation (Nigeria Re)[47] who are enabled by law to receive compulsory cessions[48] from the market. Comprehensive figures as to the amount of life insurance premiums ceded abroad by Nigeria Re were unavailable. Figures from the report of the 1986 Insurance Investigating Panel indicate that in the 1978-1983 period,[49] the Nigeria Re retained on average about 1.08% of life premiums ceded to it. For the 1978-1983 period this amounted to a little under ₦6000. It is not clear how much the Corporation received by way of overseas reinsurance acceptances. It is

47. This deduction has been made in the absence of Nigeria Re data. However since the Insurance Department, and Nigerian Insurance Year Book statistics do not include Nigeria Re life premium figures, the assumption appears to be reasonable.

48. The Nigeria Re decree requires compulsory cessions of 20% of premiums on each life policy. In practice, however, the Corporation reeived 40% compulsory cessions of all life assurance treaties and retained the right of first refusal on facultative business (Life Insurance Vol.4/90 June 1990,p.8.).

however significant that in 1988 it took a policy decision to the effect that as from January 1990, no life insurance risks would be reinsured outside the country. The reasons given for this decision to localise life reinsurance business in the country were:

(1) to conserve scarce foreign exchange resources

(2) to strengthen the local insurance market

(3) to increase the quantum of life funds for investment in the country and

(4) to build and develop reassurance expertise in the market.[50]

However the real reasons behind this sudden policy shift appeared to be based on the fact that international reinsurers were cancelling their reinsurance treaties with the market because of non-payment of reinsurance premiums due to these reinsurers. Stringent contract terms were being imposed on the Nigerian market by these reinsurers as a result of the non-payment of premiums.[51] The progressive devaluation of the Naira also rendered the business unprofitable for the international reinsurers since the premiums due to them had to be converted from local currency to foreign currency. It is unlikely that if the business was profitable in terms of the volume of reinsurance acceptances from overseas markets that the Nigeria Re would have made such a decision. The decision to localise life reassurance was not received ethusiastically by insurers in the market. The decision was seen to be impracticable because the Nigeria Re lacked the necessary expertise and capacity to implement such a policy.[52] The international reinsurers, in addition to accepting cessions from the Nigeria Re, provided ancillary services and technical assistance in such areas as product design and development, underwriting and rating, training and accounting services. Since the Nigeria Re had been dependent upon these reinsurers for these services, it is unlikely that they would be able to cope especially in view of the lack of skilled personnel in this area. The Nigeria Re would have to resort to negotiating technical assistance contracts with the foreign reinsurers.[53] This would involve

49. This panel has been referred to in chapter one. It was authorised by the Government to examine the insurance market. Despite repeated efforts it proved impossible to obtain a copy of the report. The figures quoted have been obtained from Falegan 1991,p.218.

50. As stated by the Managing Director NICON, a government spokesman. See Life Insurance ibid,p.7.

51. See "Ten Years of Professional Reinsurance in Nigeria", 1987, pp.56-59 and also WAICA Vol.XI 1987,p.153.

foreign currency disbursements overseas which could lead to increased operational costs since the international reinsurers have traditionally had the advantage in imposing contract terms.

Table 6.24
Nigerian Life Office Cessions 1977-1988

Year	Local Cessions(₦)	International Cessions(₦)	Cessions Accepted(₦)
1977	4,608,627	-	27,592
1978	1,652,647	-	360,719
1979	3,197,871	-	-
1980	926,209	1,997,554	555,852
1981	881,494	2,599,294	509,332
1982	4,646,755	-	6,074,884
1983	6,165,934	-	9,406,604
1984	6,974,786	-	4,376,004
1985	7,434,204	-	5,320
1986	10,193,727	-	-
1987	9,900,526	-	-
1988	9,316,356	-	1,506
Total	65,599,136	4,596,848	21,317,813

Source: (1) Nominal retention figures obtained from the Insurance Department (2) Retention ratio calculated from data from the Insurance Department
Notes: (1) Retention ratio is given by Gross Premiums less Premiums ceded/Total Life Premium Income % (2) Cessions accepted indicates cessions accepted locally and is presumed to include retrocessions from the Nigeria Re.

6.4 The Efficiency of the Nigerian Life Insurance Market

The government's regulatory objectives are aimed at improving life insurance market efficiency. The study of life industry market structure in the previous section has shown that the market has been characterised by a high degree of concentration, low entry rates, and a low degree of innovative activity. The establishment of the national companies has been on the basis that they were to operate as lead companies in the market and assist in raising the operational efficiency of the market. The existence of such market characteristics raises questions about the efficiency of the market. The

52. Life Insurance, ibid,p.11.

53. The Managing Director of NICON stated that "I would indeed not be surprised if [the Nigeria Re] obtain special assistance in the next few years from overseas reassurers either by means of professional fees or on special terms. It is difficult to see any way out..." Life Insurance, ibid, p.11.

traditional structure-conduct-performance model is a long-run relationship and in the long-run, structure is assumed to determine conduct and performance. The performance or efficiency of the life market may be measured in terms of cost structures, investment performance, labour productivity and the level of retentions, among other things. Of particular importance is the concept of scale economies which refers to the relationship of average costs per unit of production to the scale or size of the firm. Economies of scale represent increased efficiency of operation on the part of the firm and a determination of the minimum efficient scale of output per unit of time at which the plant or firm can realize the lowest obtainable costs of production has significant implications for the direction in which form regulatory policy towards the industry should take.

In this section, time series and cross-sectional empirical analyses regarding life company efficiency have been employed in order to examine the factors which account for efficiency among the offices.

Econometric models have been developed using the regression analysis technique. An explanation of this technique can be found in most basic econometric texts,[54] and as such a detailed analysis of this technique will not be attempted here. The application of this technique enables the relative importance of the variables selected in the analyses to be estimated. Although the specification and estimation of econometric models has been extensively used to examine the relationships among variables for life industry data in some of the industrialised countries, this has not been the case with Nigerian life industry data. This means that there is no a priori information on which to base the selection of variables and their specification. Consequently, the decisions as to the variables used and the specification of their relationships in the various models were with regard to one or more of the following; (1) the underlying economic theory, (2) a review of the related literature in which similar techniques have been applied to data in the U.K and U.S.A. (3) the judgement and beliefs of experienced managerial personnel in the Nigerian life market and (4) intuition. For the cross-sectional average cost models employed in this thesis, heavy reliance has been placed on the literature relating to cost studies conducted in western markets.[55] The other models have been developed mainly with regard to (1), (3) and (4) above.

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54. See, for example, Johnston 1987, Gujarati 1979 and Blalock 1985.

55. See for example, Houston and Simon 1970, Pritchett 1972 and 1973, Richards and Colenutt 1975, Colenutt 1977, Geehan 1977 and Pritchett and Brewster 1979 among others.

The regression coefficients have been estimated using the ordinary least squares method which assumes a linear or intrinsically linear relationship between the dependent and independent variables. The form of the model used is

$$Y_i = \beta_1 + \beta_2 X_{2t} + \beta_3 X_{3t} + ... + \beta_k X_{kt} + u_t$$

which states that at a particular point in time t, the dependent variable Y is determined by a linear combination of k-1 variables and a disturbance term u. The disturbance term represents all the variables which have not been included in the regression model for various reasons,[56] and it also reflects the intrinsic randomness in the dependent variable Y which cannot be explained. Under certain assumptions, the ordinary least squares method provides the best linear unbiased estimate (BLUE)[57] of the regression coefficients. These assumptions are as follows; (1) the mean or average value of the deviations of the disturbance term u, for any given independent variable X should be zero, (2) there is no serial correlation (autocorrelation) in the disturbances, (3) there is no correlation between the disturbances and the independent variables, (4) the variance of the disturbance term u for each independent variable X is constant, that is, they are homoscedastic and (5) each distribution term u_i is distributed normally (the normality function).

Although the independent variables may be linear (or intrinsically linear) in the regression parameters ß, they may not be linear in the variables X. In order to deal with this, in some of the models specified in this study, some of the independent variables have been transformed into their logarithmic and reciprocal forms. The models have been generated using the process of backward elimination. This was done by initially developing a model containing all the variables originally selected and dropping the variables with t-values of less than 1.

Two tailed tests of significance (t-statistic) have been conducted at 5% and in some cases 10% level of significance. The t test has been applied to the independent variables to test the various hypotheses which are discussed in the following sections. The statistical significance of the models (with regard to the variables included) have

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56. For example the theory determining the behaviour of Y may be incomplete or quantitative information about the variables may be unavailable.

57. An estimator is said to be BLUE if it is linear, unbiased and has the least minimum variance of all the possible linear unbiased estimators.

been determined by an examination of the F values generated. For all the models specified the null hypothesis (that the regression equation is not statistically significant) has been rejected at 5% level of significance. The goodness of fit of the models has been measured by the coefficient of multiple determination R^2, which measures the proportion of the total variation in the dependent variable accounted for by the independent variables. The R^2 values reported are the adjusted R^2 coefficients which take into account the effect of the addition of more independent variables to the regression model.

In situations where autocorrelation, multicollinearity or heteroscedacity are present, the ordinary least squares estimators of the regression equation may be inefficient. This means that the application of the t and F tests will no longer be valid. Detecting the presence of auto-correlation has, in the equations generated, been done by the application of the Durbin Watson test.

The Durbin-Watson (DW) statistic has been applied at 1% significance levels to time series data to test for the presence of positive or negative serial autocorrelation in the disturbance terms. For all the time series models specified, the null hypothesis of nonautocorrelated disturbances has been accepted.

Detecting the presence of multicollinearity (the existence of a "perfect" or exact linear relationship among some or all the explanatory variables) is in practice difficult. However, multicollinearity is often suspected when for a particular regression equation, the adjusted coefficient of multiple determination R^2 is high, and in addition to this, the zero order correlations are high, but very few or none of the regression parameters is significant.[58] In all of the regression equations that have been employed, these characteristics were not detected, and on this basis, the conclusion has been drawn that there were no problems of multicollinearity.

The Langrange multiplier (LM) test has been used to test the time series models for the presence of heteroscedasticity. The test is distributed as a chi-squared variate with one degree of freedom. In all the models the null hypothesis of homoscedasticity was accepted. The test for normality is based on a test of skewness and kurtosis of residuals. The assumption of normality assumes normally distributed u_i's with zero mean, constant variance and covariance of zero among the residuals. the test is

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58. See Gujarati 1979,pp.181-182.

distributed as a chi-square variate with two degrees of freedom. Its importance lies in the fact that it simplifies estimation and testing of linear regression models. In all the models tested, the null hypothesis (the assumption of normality) was accepted.

6.4.1 Average Costs and Economies of Scale

The relationship between the average costs and life premium income of the life offices has been examined in order to investigate the existence or otherwise of economies of scale. This relationship is of particular importance because of the nature of Nigerian life industry structure, that is, an oligopolistic market with low entry rates. Some of the questions to be considered is whether the existence of economies of scale are responsible for the low entry rates in the market, and whether the larger offices are more cost efficient than the smaller ones. Apart from this, the importance of costs lies in the fact that life office estimate future expenses in order to actuarially determine the premiums to be charged on various policies. The higher the estimate of future costs (which are in part dependent upon historical costs and expectations of inflation), the higher the premium the policyholder is charged. Thus, cost inefficiencies in the market will raise the effective cost of life insurance to prospective policyholders. There are various measures that can be used to measure the size of life offices, such as premium income, sums assured in force and size of the life fund. These measures have been said to be of limited value in estimating costs because they do not consider many of the variables that influence operating expenses.[59] It has been however argued that premiums are more representative of an insurers importance in the market and as such this size measure has been used.[60] Since the linear form of the size variable was considered a poor fit, three transformations of the size measure for premiums were employed, the logarithmic, reciprocal logarithmic and reciprocal transformations. In each case the results of the function which estimated the parameters best have been reported.

In the regression model generated, average costs (AC) have been defined as total operating costs (OE) which include management expenses, commissions paid and other expenses divided by total life premiums, and LP denotes life premiums. Other important variables apart from the size variables have also been considered to control

59. See, for example, Pritchett 1971. Pritchett argued the case for using Actual/Standard expense ratios which is said to be "reasonably reliable for intercompany comparisons of operating expenses." See also Pritchett, 1973 and also Geehan 1985.

61. See, for example, Colenutt 1977.

for differences among the life offices. These are, the rate of company growth, ownership structure and corporate form. A life office which is growing is likely to have higher costs because of commission payment arrangements. Commissions paid on new business underwritten usually constitute a high percentage of first year premiums. In order to control for this, a variable NP/LP, first year premiums divided by total premiums has been included. This should be positively correlated with average costs.

One of the main objectives for the restriction of the activities of foreign offices and the establishment of national companies was to improve market efficiency. Since the differences in ownership are qualitative rather than quantitative, dummy variables are used. The general rule is that if a qualitative variable has m categories, only m-1 dummy variables should be introduced into the model. Since there are three possible categories of dummy variables, FOR for foreign life offices, NAT for national life offices and IND for indigenous life offices, only two dummy variables, FOR and NAT, have been included to investigate economies of scale among the different offices. These took the value of 1 for foreign companies and 0 otherwise and 1 for national companies and 0 otherwise. NAT has been defined as wholly, that is, 100% owned by the government, while FOR denotes companies with some degree of foreign equity. From the point of view of regulatory objectives, the national companies should show evidence of economies of scale, and as such NAT should be negatively correlated with average costs.

The form of the offices might influence average costs. To determine whether there is any significant difference in costs associated with corporate form, a variable, COMP, which takes the value of 1 for composite offices and 0 otherwise, has been included.

The following regression models were generated for the 1981 and 1988 data: A simple regression model;

$$OE = \beta_1 + \beta_2 LP \qquad [1]$$

and a multiple regression model;

$$OE = \beta_1 + \beta_2 LP + \beta_3 NP/LP + \beta_4 FOR \qquad [2]$$

All the variable definitions are presented in table A13 in appendix A.

One of the aims of the analysis is to compare estimates of the regression model in two different regulatory periods, in order to determine whether economies of scale existed in the different periods defined. In order to do this, it was considered necessary to compare cross-sectional data in these periods. The principal legislations relevant for this analysis came into operation in 1976 and 1977[61] and 1976/1977 should therefore serve as a benchmark period for comparing the cost structures of life offices in the market. However, micro data, that is individual company data, for the period before 1981 were unavailable. As a result 1981 data have been used. Although this might be seen as a limitation in the analysis, this is not expected to detract from the analysis, if the effects of regulatory lag are taken into consideration. Thus a regulatory lag period of about 4 years (from 1977) has been assumed. This appears to be reasonable, especially in the Nigerian situation, where it takes some time for regulation to be enforced.

The data used was obtained from the returns of insurance companies to the Insurance Department in Lagos. For the 1981 regression a sample of 18 life offices (out of the total of 25 for which returns were available) have been used. Seven companies were left o ut of the analysis because their cost data were unavailable or insufficient. The 1988 sample contained 26 out of the 33 companies in the market. The offices excluded from the analysis were

(1) companies that had been operating in the market for less than 10 years since the start up expenses of newly established companies are expected to be high in the first years of business,

(2) companies transacting reinsurance business exclusively since they do not operate in the same market with the direct offices,

(3) Companies for which the data were unavailable or insufficient. All the companies in both samples utilised both the agency method and direct selling method in the distribution of life insurance products.

The results of the 1981 and 1988 regressions analysis are presented in table 6.25. Two regressions were run for each year. The first regression is a simple regression model which estimated the function using the size variable as the independent variable.

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62. The Insurance Decree 1976, the Nigerian Enterprises Promotion Decrees 1977 and the Nigerian Reinsurance Corporation Decree 1977.

These models are denoted by OE11 and OE81 for 1981 and 1988 data respectively. The variable 1/LogLP, denoting the reciprocal logarithmic transformation of the life premium, was used in the 1981 regressions. If economies of size were present it is expected that the coefficients on the reciprocal logarithmic premium transformations would be positive.

OE11 and OE12 indicate the presence of economies of size in 1981. Introducing the variables NP/LP for new business underwritten and FOR for foreign life offices into the simple regression increased the explanatory power of the model by over 100%. Since the constants in both functions were positive, this indicates that the average costs decreased with size in a non-linear form. As expected the coefficient for new business underwritten which has been used as a proxy for growth was positive, suggesting that the offices growing rapidly have higher costs. The coefficient for foreign life offices was positive and statistically significant, indicating that for this category of life offices, expenses increased with size. The results suggest that the foreign companies were operating at higher cost levels than the other companies. Although the variables for national and composite life offices were initially included in the model, they were dropped due to lack of significance.

Figure 6G displays the relationship between average cost and firm size. It illustrates the variation in cost structures among the various companies in the 1981 sample. The presence of economies of scale would suggest that the larger companies (in this case those nearer the 0 coordinates on the Y axis since the reciprocal values of the log transformation of life premiums has been used) should experience lower average cost levels compared with the relatively smaller ones. However, only 3 of the largest 5 firms had average cost values lower than 20%, while the lowest average cost (10.9%) was obtained by a company that would be classified as relatively small. In fact the average cost figures for the largest 7 companies ranged from between 12-60 (%). The explanation for this probably lies in other factors such as the growth and ownership factors which are associated with higher average costs.

Table 6.25
Cross-Sectional Average Cost Regression Analysis
1981 & 1988

VARIABLES	1981 OE11	1981 OE12	1988 OE81	1988 OE82
Constant	-43.01	-86.67	38.51	37.38
	(-1.45)	(-3.17)*	(9.77)*	(2.96)*
LogLP				
1/LogLp	473.70	666.70		
	(2.57)*	(4.17)*		
1/P			6693008.00	6196698.00
			(3.15)*	(2.55)*
NP/LP		0.17		-0.03
		(2.02)**		(-0.22)
FOR		22.54		-2.39
		(3.11)*		(-0.25)
NAT				3.53
				(0.38)
COMP				1.95
				(0.16)
S	15 98	12.86	17.18	18.58
R^2	24.70	51.20	26.40	13.80
F	6.58~	6.96~	9.95~	1.80

*t-statistic significant at 5%
**t-statistic significant at 10%
~F value significant at 5%

For the 1988 data, the reciprocal transformation of the life premiums were used in estimating the regression function. The simple regression model OE81 suggested the existence of economies of scale, with average costs decreasing with increases in size in a non-linear manner. The expanded model OE82 also indicates economies of scale, however, the addition of the ownership variables FOR and NAT, the structure variable COMP and the proxy for growth NP/LP decreased, rather than increased the explanatory power of the model since none of them was statistically significant. In fact the multiple regression model was statistically insignificant at 5% level of significance. Thus size accounted for a little over one quarter of the variation in average costs, while ownership was not a significant factor. This means that there could be some other variables which have not been included in the model which may account for the existence of economies of scale. An example is the quality of management, since good managers could be successful in controlling costs. However, since there was no way of estimating this effect, it could not be included in the model. Another factor could be the proportions of the various categories of life insurance policies underwritten by the various life offices, since different kind of policies have different associated costs.

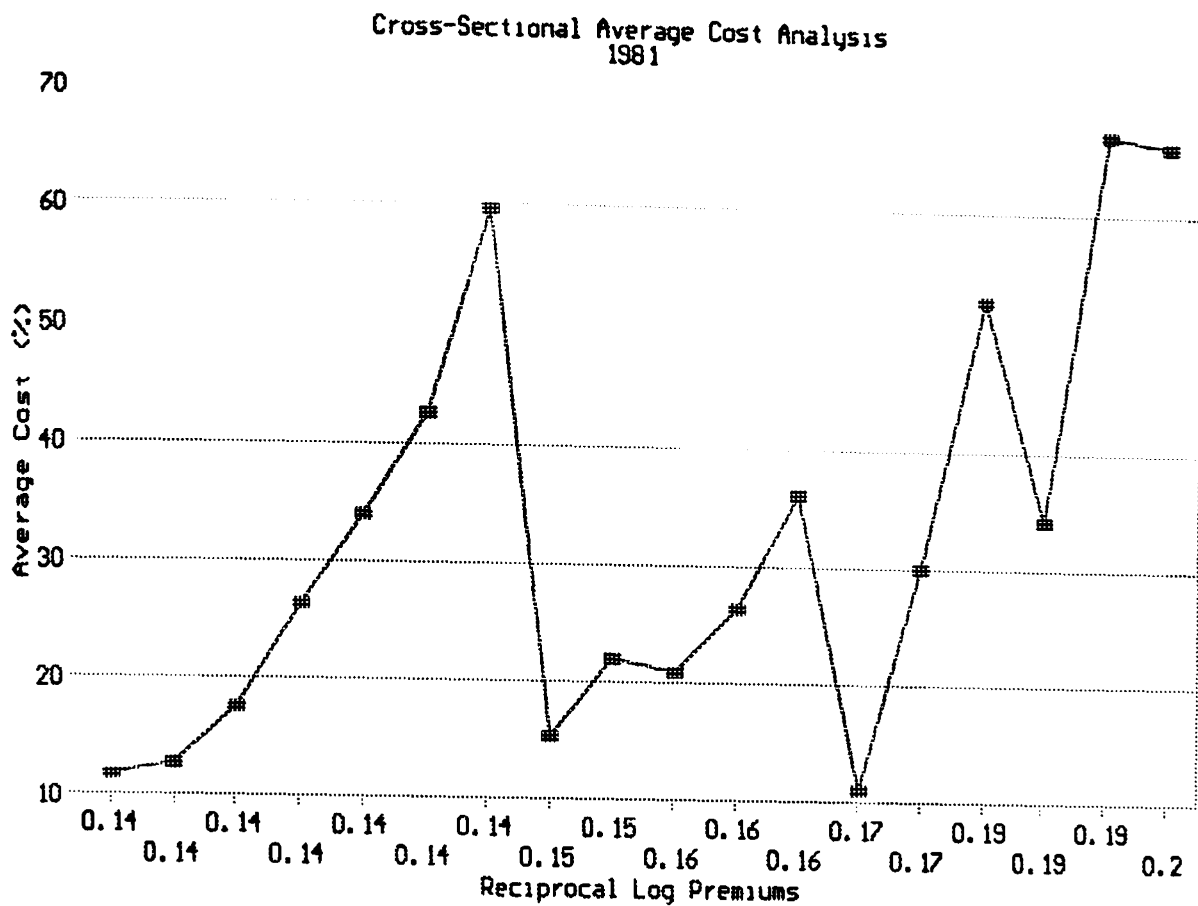
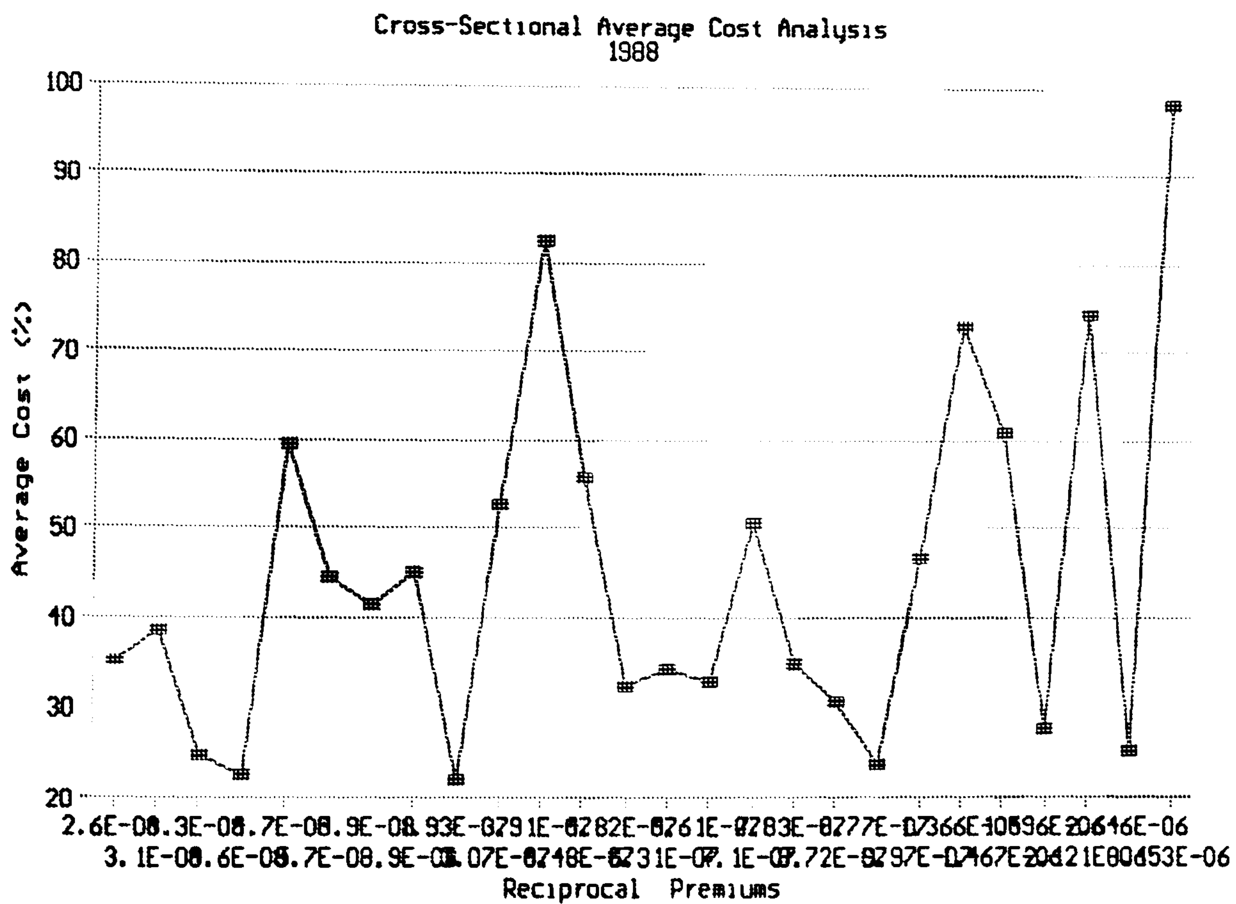


Figure 6H



Since the relevant information was not available, this also could not be included in the model. In addition to this, buyer preference could be an explanatory factor in the sense that potential policyholders are attracted to the bigger life offices because of the perceived quality of their products as compared with the other fringe life offices. This could stimulate economies of cumulative volume so that costs decline over time as a result of the learning or experience-curve effect. An estimate of the optimum size of company for this sample using the survivorship technique (see section 6.2.3) suggests that optimum size is achieved at premium incomes of N15 million and above. Only the largest 7 companies achieved this level of premium income. Although 8 of the largest 10 companies experienced average cost levels of less than 45%, quite a number (8) of the relatively smaller ones had average cost values of less than 35% (see figure 6H). This has implications for cost efficiency and suggests that although there is evidence for the existence of economies of scale, companies are not operating at minimum efficient scale.

Although comprehensive reliable information on prices, that is, premiums charged by the various offices is not available, market sources suggest that these are high.[62] This presents implications for the efficiency of the market. If the relatively bigger life offices, especially the top ten offices are charging high premiums despite the evidence for economies of scale, it would appear that policyholders are not getting a good deal. If the cost inefficient firms are also charging high rates, this would also contribute to market inefficiency because of the umbrella effect, where the inefficient firms are shielded because of the high costs being charged by all firms in the market. The positive correlation between market share and profitability has been investigated and established in a number of studies.[63] Therefore the large market shares of the bigger life offices (the top four life offices control over 50% of total life market premiums while the top ten offices control about 95% of the market), coupled with high premium rates in addition to scale economies lead to the conclusion that the relatively bigger life offices are more profitable than the others. The non availability of reliable operating profits data made it impossible for the hypothesis to be tested in this specific case but in the light of the available data it appears reasonable to make this conclusion.

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63. Information obtained during discussions with industry senior managerial personnel during May-July 1991.

64. See for example, Buzzell et Al 1975; Bradley and Branch 1982 and Buzzell and Gale 1987. The data for these studies were obtained from the PIMS (Profit Impact of Market Strategies) database of the Marketing Science Institute. The hypothesis that market leadership is the primary determinant of profitability has however been challenged. See Woo and Cooper 1982 and Woo 1984.

Two time series models were tested to examine the movements in average costs over the years. The first model (AC1) examined the trend from 1977-1988, while the second model (AC2) examined the trend from 1979-1988. The operalisation of the models is as follows:

$$AC1 = \beta_1 + \beta_2 \, LogLP_{t-1} + \beta_3 \, MIL + \beta_4 \, OIB \qquad [3]$$

$$AC2 = \beta_1 + \beta_2 \, LogP_{t-1} + \beta_3 \, NB_{t-1} + \beta_4 \, GP_{t-1} + \beta_5 \, LR_{t-1} + \beta_6 \, MIL \qquad [4]$$

For the time series data average costs were defined as all the expenses of management less commission payments divided by total life premiums. In both models the independent variables have been lagged by one period to take into account the lapses of time before the industry responded to the exogenous variables, that is, the shocks in the environment. MIL and OIB and are dummy variables. MIL takes the value of 1 when the country was under military rule and 0 otherwise, OIB takes the value of 1 during the era of economic prosperity (the oil boom years), and 0 otherwise. A dummy variable $DEC59^{+4}$ was initially introduced into the model to account for the four year period after implementation of the 1976 Insurance Decree, the 1977 Nigeria Re Decree and the 1977 Nigerian Enterprises Promotion Decree. The purpose was to determine whether economies of scale existed during this period of regulatory lag. The t-statistic on this variable was considerably less than one in all the transformations of the model, and as such it was dropped. The qualitative values of all the dummies used for both time series analysis are their midyear values.

If economies of scale existed during this period, it is expected that the signs of the regression coefficients for the size variable Log LP_{t-1} to be negative. The sign of MIL is expected to be positive because the greater part of this period coincided with increasing inflationary trends in the country, with rising consumer prices. During the oil boom era, consumer prices were still relatively lower and as such OIB is expected to take on a negative sign.

AC2 takes into consideration the lagged variable NB_{t-1} (the proxy for new business underwritten or growth). It is expected to take on a positive sign indicating the high costs associated with increased new business. Life offices sell various products which have different associated costs. Industrial insurance is high cost business while group life business is low cost. In order to control for this effect, a variable GPt-1, (which

has been lagged by a year) for group life insurance, has been introduced into the regression. It should be negatively correlated with average costs.

Lapse ratios, the amount of life insurance lapsed divided by total life premiums, are an important determinant of average costs. If policies are lapsed during the early years of the contract, this could increase the costs of the company since acquisition costs might not have been recovered. This variable LR_{t-1} (also lagged) is thus expected to be positively correlated with costs. It would have been ideal to introduce the preceding variables into the 1977-1988 regression, but the data were unavailable and as such this was not possible.

Table 6.26
Time Series Average Cost Regression Analysis
1977-1988

VARIABLES	ME1	ME2	ME3
Constant	103.76 (2.05)		20.21 (8.04)*
$LogLp_{t-1}$	-10.57 (-1.66)		
$1/logLp_{t-1}$		13.20 (0.41)	
1/pt-1			-75255160.00 (-0.35)
MIL	8.06 (4.13)*	6.14 (2.88)*	5.59 (2.94)*
OIL	-12.51 (-3.53)*	-7.90 (-2.39)*	-7.19 (-3.23)*
S	2.16	2.55	2.53
R^2	71.00	59.70	60.20
Dw	2.12+	2.12+	2.13+
F	9.14~	5.94~	6.02~
LM[1]	1.4033^	0.74059^	1.5546^
N[2]	0.490^^		

*t-statistic significant at 5%
~F value significant at 5%
+Durbin Watson test applied at 1% significance level
^LM test at 1 degree of freedom, 5% significance level
^^ Normality test at 2 degrees of freedom

Table 6.27
Time Series Average Cost
Regression Analysis 1979-1988

VARIABLES	ME
Constant	50.87
	(4.16)*
NB_{t-1}	7.12E-04
	(7.88)*
GP_{t-1}	-0.38
	(-3.18)*
$LogLP_{t-1}$	0.06
	(0.06)
LR_{t-1}	-1.54
	(-6.58)*
MIL	4.82
	(5.98)*
S	0.68
R^2	97.20
Dw	2.57+
F	49.46~
LM[1]	1.1488^
N[2]	^^

*t-statistic significant at 5%
~F value significant at 5%
+Durbin Watson test applied at 1% significance level
^LM test at 1 degree of freedom, 5% significance level
^^Too few observations to compute test statistic

The results are presented in tables 6.26 and 6.27. In both models there was no evidence of the existence of economies of scale over the relevant time periods. For model AC1 the regression containing the logarithmic function of size, LogLp, has a greater explanatory power than the other transformations, although in terms of significant t-statistics, the results are basically the same. Although the regression coefficient for size was negative, it was not significant. As expected, costs were high during military rule and low during economic prosperity. Model AC2 has greater explanatory power than AC1. In Model AC2, new business was found to be positively correlated with average costs, which confirms the hypothesis that new business growth is associated with increased costs, and as expected a high proportion of group life business results in lower costs. The coefficient for lapse ratio is however unexpectedly negative. This could be for a number of reasons. First, lapses could have occurred after the policies had been in force for a period long enough for all the associated acquisition costs to have been recovered. Second, since the management expenses do not include commission expenses, this could have had the effect of reducing the impact of lapses on average costs. As expected, costs were high during the military period.

Figure 6I

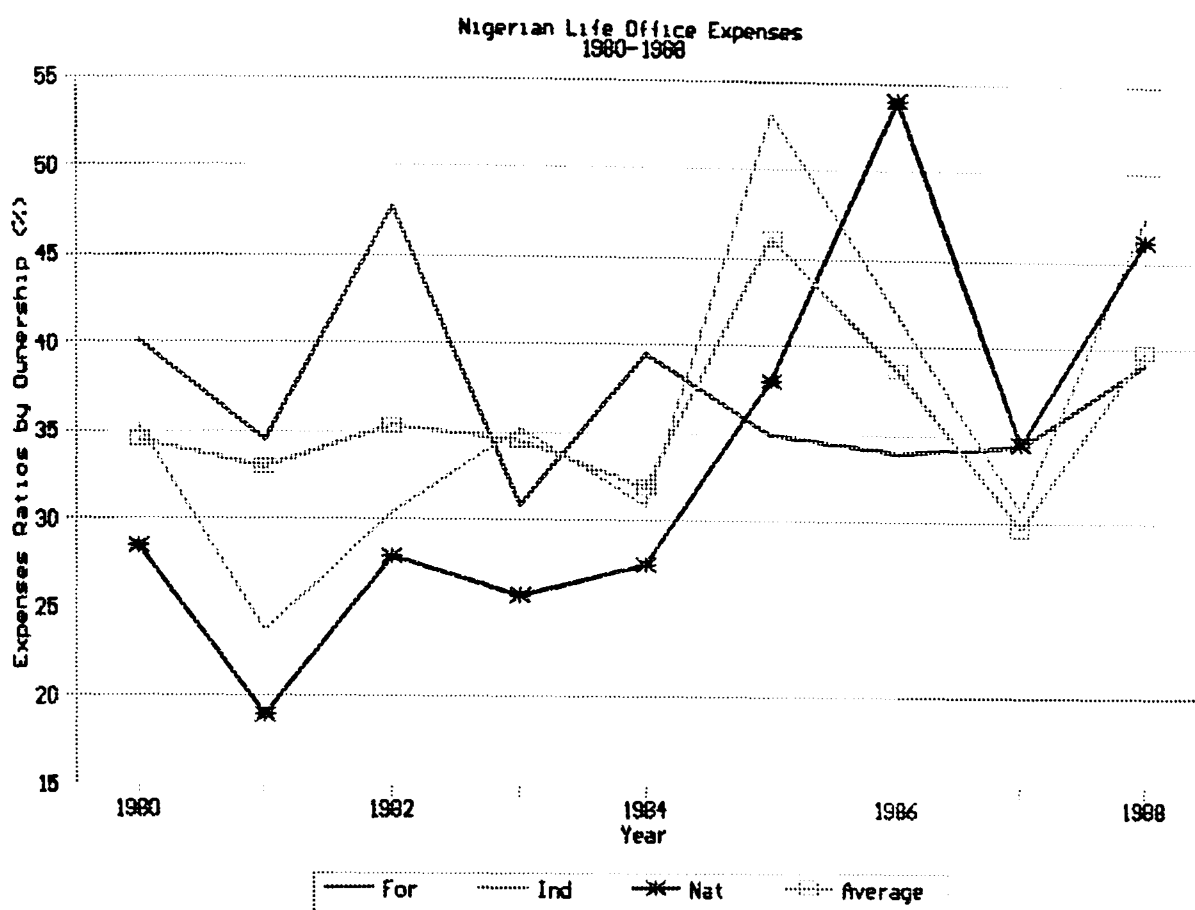


Figure 6I shows the differences in expense ratios for a sample of six foreign,[64] five indigenous[65] and six national[66] life offices over the 1980-1988 period. This sample will be referred to as the control sample. The life offices were selected on the basis of availability of the relevant data over the period and the sample contained the same offices over the period with the purpose of seeing the pattern of changes in expense ratios over the period. Foreign office expense ratios were on average higher than both the average total market ratios and those of the other categories of life offices.[67] However, Figure 6I indicates that although the foreign life offices average ratios were higher, since 1985, they were on average lower than the national and indigenous life offices whose expense ratios rose to a peak of over 50% of premium receipts in 1985 and 1986 respectively, at a time when the foreign life offices were keeping their expenses down. Although expenses appeared to drop around 1985, since 1987, they have been on the increase. Expenses figures from the Insurance Department show that the drop in expenses was mainly attributable to a decrease in commissions payments

65. The African Alliance, American International, British American, Crusader, Lion of Africa, and Royal Exchange.

66. The African Prudential, Marine and General, Rivbank, United Nigeria Life and Unity Life and Fire.

67. Bendel Insurance, Gateway, Great Nigeria, NICON, Niger and Nigerian General.

to agents and other costs associated with the payment of agents on a non-commission basis (table 6.28).

Table 6.28
Distribution of Life Office Expenses
1977-1988 (₦'000)

Year	Agents Commissions	Management Expenses	Agents Compensation*
1977	6572	10077	-
1978	7578	12771	-
1979	8035	11080	-
1980	11563	18492	54
1981	14393	22046	64
1982	12459	19678	1386
1983	14543	25845	2026
1984	13254	28182	1691
1985	14069	32908	2213
1986	22448	45462	54
1987	17571	41240	2695
1988	22598	50345	2199

*compensation to agents other than commissions payments

Table 6.29
Labour Productivity and Wage per Employee
in the Nigerian Life Market 1987-1988

Year	1987		1988		1987-1988	
	LP/SL	ME/SL	LP/SL	ME/SL	LP/SL	ME/SL
FOR	42093.6	7875.6	39662.2	9041.1	40877.9	8058.4
IND	7523.8	4334.3	6784.9	3711.8	7154.4	4023.1
NAT	22738.8	4959.3	38240.9	5595.5	30489.9	5277.4

Since management expenses formed the greater part of the operating expenses of the life offices, the nature of the expenses of the various categories of life offices was analysed to determine whether the variation in expense ratios was due to variations in salary structure among the different categories of life offices. It was expected that salaries per employee would be higher in the foreign and indigenous life offices, since salaries in the national companies were paid in line with the civil service salary structure which is lower than private sector salaries. The life office returns at the Insurance Department did not differentiate between salaries and other categories of management expenses, and as such management expenses has been used as a proxy

68. The expense, claims, investment and retentions data of the companies by class of ownership are reproduced in appendices A7 to A11.

for salaries. The estimate of average salary, or salary per employee has been defined as the ratio of management expenses to size of labour force. Since size of labour force data was unavailable for the years 1980-1986, estimates for the two years 1987-1988 were made and the figures averaged. The average estimate figures show that as expected, salaries per employee were higher in the foreign life offices compared with the national and indigenous offices (table 6.29). In order to determine whether the higher salaries paid in the foreign offices was justified, labour productivity LP/SL (the total life premium income divided by the size of the labour force) was calculated for all categories of the life offices. The data indicated that labour productivity was higher in the foreign life offices. The two values were correlated and found to be positively correlated with a coefficient of 0.851. The implication is that the higher foreign life office management expenses is justified. The direction of the relationship is however unclear, that is, whether higher salaries result in greater productivity or vice versa.

6.4.2 Claims Payments

Claims costs are a significant proportion of life office expenses. Life offices endeavour to keep their claims ratios low so as to improve efficiency and profitability. Policyholders interests are served when, all things being equal,[68] a high proportion of their premiums is returned to them in the form of claims payments. This is especially true in the Nigerian situation where policyholders complain about the offices inability or reluctance to compensate their policyholders.

A regression model was initially developed with the independent variables of size and type of ownership of life office in order to investigate the direction of the relationship between claims and these variables. This however did not yield any significant results, and finally a simple regression model of the form

$$\text{Claims} = \beta_1 + \beta_2 \, LP \qquad [5]$$

was developed. In order to determine the form of the relationship between size and claims, three transformations of the independent variable LP (life premiums) have been undertaken. The independent variables LogLp, 1/LogLp and 1/Lp were used in

69. This assumes the principles of insurance pricing (adequate, non-excessive and non-discriminatory rates) are being adhered to.

the regression and the dependent variable claims is the amount of claim payments divided by total life premium income. If economies of scale in claims exist, then the coefficient of LogLp would be expected to have a negative sign, and the coefficients 1/LogLp and 1/LP positive signs. The results indicate that there are no economies of size with respect to claims payments (table 6.30).

Table 6.30
Cross-Sectional Claims Payment Regression Analysis
1988

VARIABLES	Claims1	Claims2	Claims3
Constant	-35.58 (-1.87)	59.36 (3.02)*	14.04 (5.88)*
LogLP	7.35 (2.50)*		
1/LogLP		-303.20 (-2.43)*	
1/P			-2339804.00 (-1.82)**
S	9.88	9.90	10.00
R^2	17.40	16.40	8.50
F	6.26~	5.91~	3.31~

*t-statistic significant at 5%
**t-statistic significant at 10%
~F value significant at 5%

The explanatory powers of the functions are however low, with the loglinear transformation LogLP exhibiting the greatest explanatory power (17.4%). This result suggests that there are other factors which account for the level of claims payments among the life offices. These could be such factors as mortality experience and the relative proportions of the various types of policies sold. This information was however unavailable. The results suggest that claims payments increase with size of company. The size of the regression coefficient is however small and as such it is doubtful whether this really implies increased return of premiums paid to policyholders.

A time series model shown below was developed

$$\text{Claims} = \beta_1 + \beta_2 \,\text{LogLp} + \beta_3 \,\text{MIL} + \beta_4 \,\text{OIL} \qquad [6]$$

The model was initially specified with the variable DEC59+4 in order to determine the direction of the relationship between claims ratios and the period of the regulatory lag. The t value for this variable was however less than 0.1 and it was dropped from the final model.

Table 6.31
Time Series Claims Cost
Regression Analysis 1977-1988

VARIABLES	Claims
Constant	-47.25
	(-0.83)
LogLp	7.43
	(1.05)
Mil	6.43
	(3.51)*
Oil	-8.95
	(-2.38)*
S	2.06
R^2	87.00
Dw	2.39+
F	25.51~
LM[1]	2.8714^
N[2]	0.495^^

*t-statistic significant at 5%
~F value significant at 5%
+Durbin Watson test applied at 1% significance level
^LM test at 1 degree of freedom, 5% significance level
^^ Normality test at 2 degrees of freedom

The results show that claims ratios increased in the military period and decreased during the era of prosperity. The claims figures appear to indicate that the decrease in the OIL era might simply be as a result of increasing premium income in this period and not necessarily as a result of decreasing claims payments. The decreasing economic activity during the latter part of the military period specified in the study possibly resulted in more policies being lapsed/surrendered as a result of decreasing amounts of personal disposable income.

A comparison of claims ratios for the control sample shows that over the period the national life offices had the highest claims ratios in the life market, an average of 27.9% higher than the market average of 16.8%. The foreign offices average claims results (12.9%), although much lower than the national offices were more stable. This could mean either of two things. (1) The national offices are more policyholder interest oriented since they have higher claims ratios, or (2) The foreign offices by prudent underwriting procedures have been able to obtain better results on their

portfolio of business and as such keep claims expenses down. The claims figures of the various categories of life offices were analysed in order to determine which of the above applied. This was done by estimating the percentage of surrenders/lapses in the claims portfolios of the life offices. If the percentage of surrenders in the portfolios of the national offices is high, this means that their high claims ratios are not in the policyholders interest because (1) this would be indicative of their inability to retain their life accounts (2) high surrender/lapse ratios are expensive and generally lead to increased costs which are eventually passed on to policyholders.

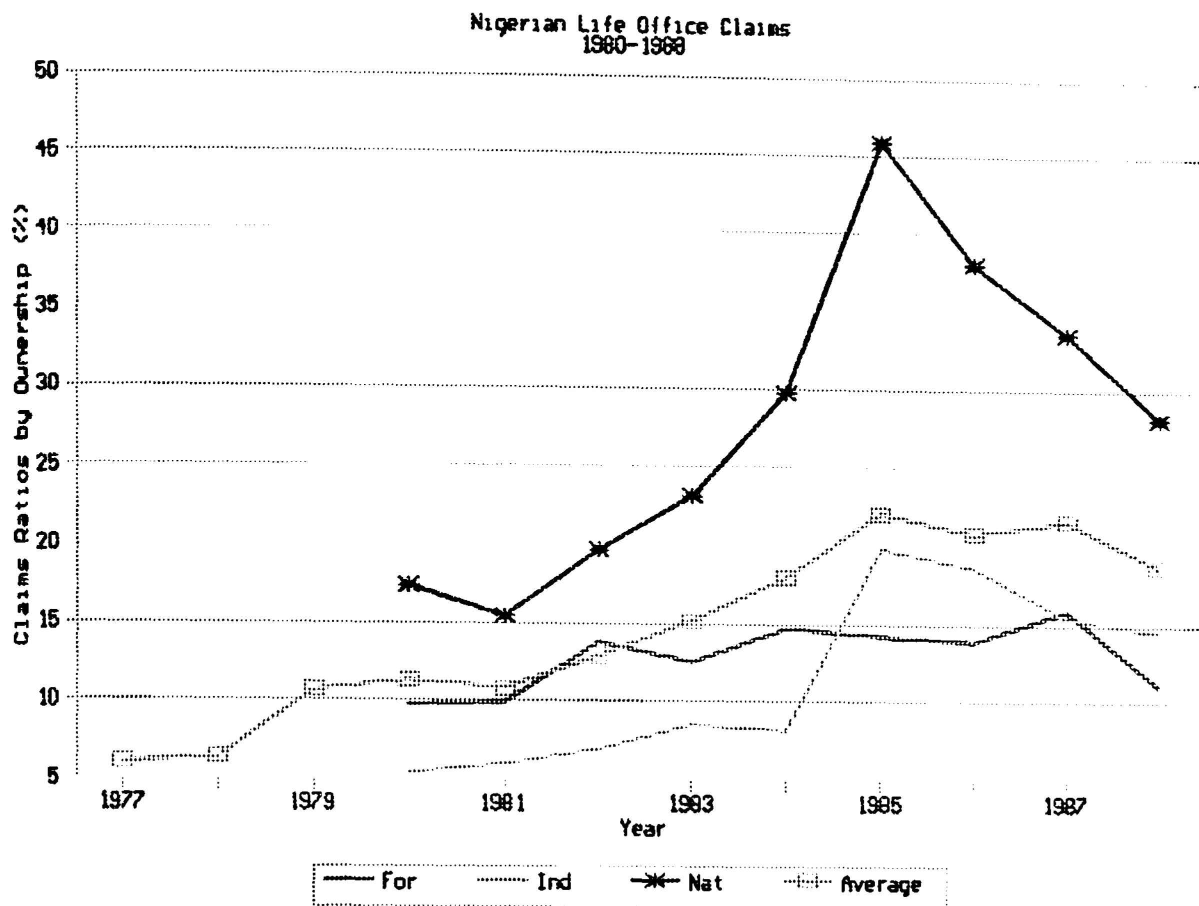
Table 6.32
Nigerian Life Offices Claims Analysis by Ownership 1980-1988

Year	FOR	IND	NAT
1981	47.2	66.3	35.9
1982	42.7	47.4	28.6
1983	44.9	67.0	8.3
1984	43.8	50.7	8.5
1985	47.9	37.4	23.6
1986	47.1	55.3	8.8
1987	51.5	55.6	23.3
AVG	39.6	54.2	19.6
STD	16.4	9.7	10.3

Note: AVG and STD denote mean and standard deviation respectively.

The results are reported in table 6.32. The 1981 and 1988 values are not included because in these two years, surrenders were not differentiated from the total values of the claims paid and as such their values as a percentage of claims paid could not be estimated. On average, the national offices had the least percentage of surrenders as a percentage of their claims portfolio (19.6%), while the indigenous life offices had the highest (54.2%). The fact that the national life offices had the least percentage of surrenders suggests that although their claims ratios were high, their claims experience has been in the policyholders interests since most of these payments were actually made to policyholders as maturity or death payments.

Figure 6J



6.4.3 Investment Performance

The investment performance of life offices is of utmost importance because of the nature of their liabilities, which are mainly long-term. In order to build up a fund from which future claims payments will be made, life offices must generate sufficient return on their invested assets, as well as make an underwriting profit. An attempt was made to generate cross-sectional models for the 1981 and 1988 data to examine, among other things, the variation in investment performance according to the ownership of the life offices, and the effects of government regulation and control of life office investments. One of the objectives was to test the effects of size or market share influence on profits. These however did not yield any significant results with respect to the size and ownership variables and variables GS/TA BS/TA, RE/TA and L/TA which represent the amounts invested in government stocks, private stocks and bonds, real estate and loans to policyholders.

However a times series model was developed which yielded some significant results. The form of the model was

$$ROA = \beta_1 + \beta_2 \, GS/TA + \beta_3 \, BS/TA + \beta_4 \, MIL + \beta_5 \, OIB \qquad [7]$$

Investment performance ROA has been measured as the pre-tax investment income of the life offices divided by total life market investment assets.

It has been suggested in the literature on Nigerian insurance market investment behaviour that the Government's regulation of the investment behaviour of insurance companies affects their investment performance because portfolio managers do not have the advantage of flexibility in designing their investment portfolios. The two variables GS/TA and BS/TA were included in the model and since the return on government stocks is relatively much lower than the return on bonds and shares, the expectation was that GS/TA should be negatively correlated with, and BS/TA positively correlated with the return on investment. During the period of economic prosperity the variable OIB was expected to be positively correlated with the return on assets. During military rule the rate of return on invested assets was expected to be negatively correlated with investment performance, as a result of the effects of the structural adjustment programmes in the economy for most of this period.

The model was initially regressed with the dummy variable $DEC59^{+4}$, but since its t statistic was less than one, it was dropped from the final regression. The results of the regression (shown in table 6.33) show that surprisingly, the sign of the regression coefficient for government stock was positive, indicating that higher amounts invested in government stocks had a positive effect on the return on investment. In retrospect however, this could be attributed to the fact that by law the life offices were required to invest at least 25% of their portfolio in this category of investments. Since the financial markets were narrow, many life offices invested more than the prescribed minimum in these assets. Thus the higher amounts of funds invested in government stock relative to the other financial instruments, would compensate for the low return on the assets.

Unexpectedly, ROA was found to be negatively correlated with OIB and positively correlated with MIL at 90% level of confidence. This raises some questions, since it suggests that the performance of the investment portfolio decreased during a period of economic prosperity when the return on investments was expected to be high. It could be argued that this has been caused by the low yields on government stock in the life offices investment portfolios. However the analysis has established a positive relationship between the variable GS/TA and ROA. This raises questions as to the efficiency of the life offices with respect to their investment practices. Cross-sectional

analyses could have presented a clearer picture, but as mentioned previously, no meaningful models could be generated from the available data.[69]

Table 6.33
Time Series Investment Income
Regression Analysis 1977-1988

VARIABLES	ROA
Constant	1.67
	(0.56)
GS/TA	0.14
	(2.22)*
BS/TA	0.07
	(1.18)
MIL	0.91
	(1.74)**
OIB	-1.87
	(-2.34)*
S	0.55
R^2	83.60
Dw	2.33+
F	14.99~
LM[1]	2.8714^
N[2]	0.495

* t-statistic significant at 5%
** t-statistic significant at 10%
~F value significant at 5%
+Durbin Watson test applied at 1% significance level
^LM test at 1 degree of freedom, 5% significance level
^^ Normality test at 2 degrees of freedom

The coefficient for the variable MIL was unexpectedly, positive. This when examined in retrospect may not be surprising.

There are two possible explanations for this. First, the life offices could have performed so well during the initial period of military rule in the country which ended in 1979, and this could have offset low investment returns in the succeeding military period (1984-1988). Second, the measures taken by the Military Government in

70. A pattern has been observed with respect to the micro data on profitability obtained from the returns of insurance companies; operating profits were either incomplete or looked suspiciously inaccurate and thus unreliable. Information from some market sources indicate that for reasons of taxation and confidentiality, some companies do not declare accurate returns in this area. As one source put it, "there are three separate sets of accounts, one for the tax office, one for the Insurance Department and the 'real' one for the company's records." This has made meaningful analysis in this area very difficult, if not impossible. The suspicion is that some of the life offices declare lower returns than what is actually obtained. On the other hand it could be argued that the data, although supplied to the Insurance Department has not been compiled accurately. Examination of the data does indeed indicate that this is sometimes the case. If this view is taken however, the assumption is that the regulatory agency personnel responsible for the compilation of returns somehow have an "aversion" to profitability data!

respect of the deregulation of the economy could have raised interest rates on the various financial instruments to the extent that the investment performance of the life offices considerably improved at this time.

The data[70] for the control sample for this period shows that indeed the average life market investment performance did improve at this time. In addition to this, in real terms the quantity of foreign life office assets exceeded that of the national and indigenous life offices, with the indigenous offices having the least assets. On average, the foreign life offices contributed almost half of the invested funds in the life market. Total life market investments rose in real terms between 1977 and 1982, but they have been declining since 1985. In terms of investment performance, again, on average the national offices achieved a slightly higher rate of return on their assets, 8.7% as compared to the life offices 8.5%. However, as in the case of the expenses and claims results, the foreign life office investment performance figures displayed less volatility than that of the national offices. The data shows that since 1985, the foreign life offices performance was improving, while the results for the national companies showed a decline.

71. The 1983 individual company assets figures were missing from the returns files and these have been estimated by extrapolating the data.

Figure 6K

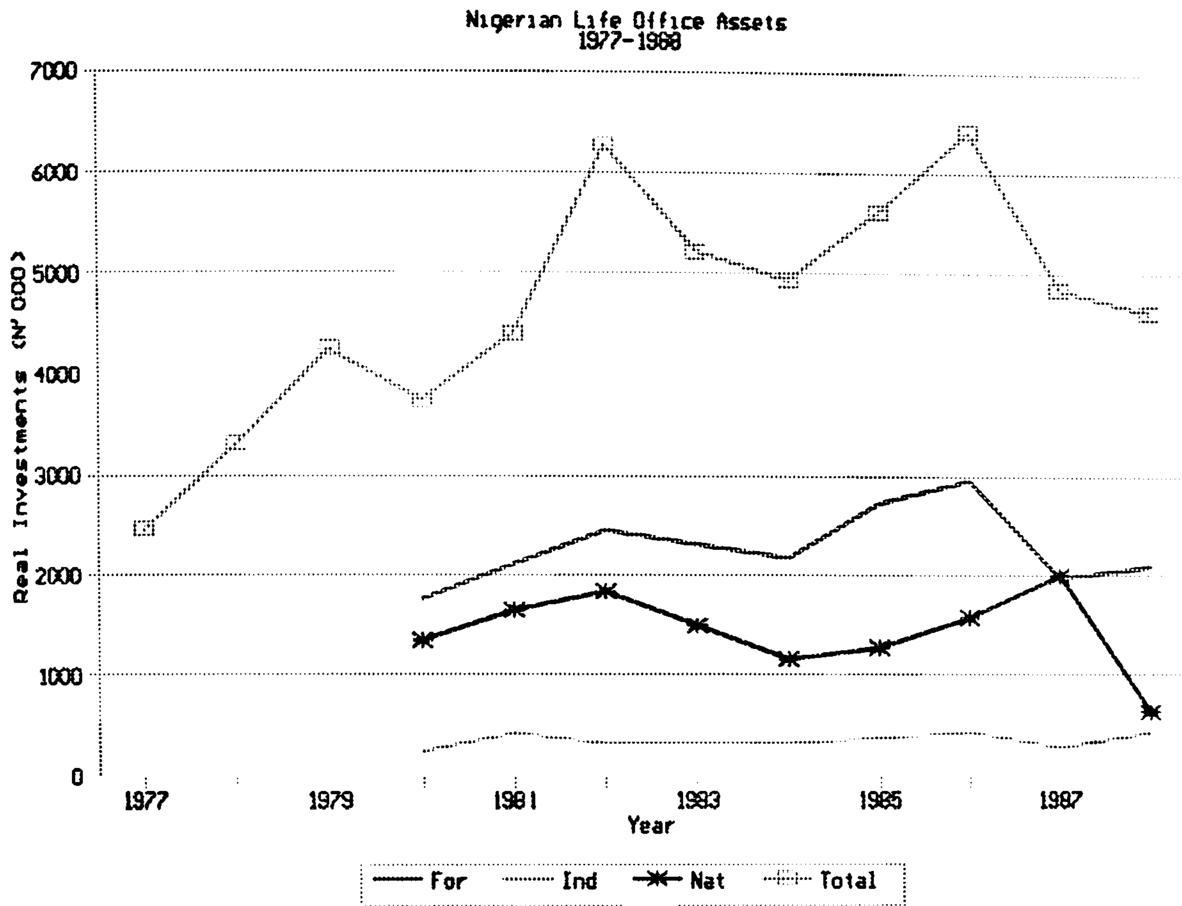
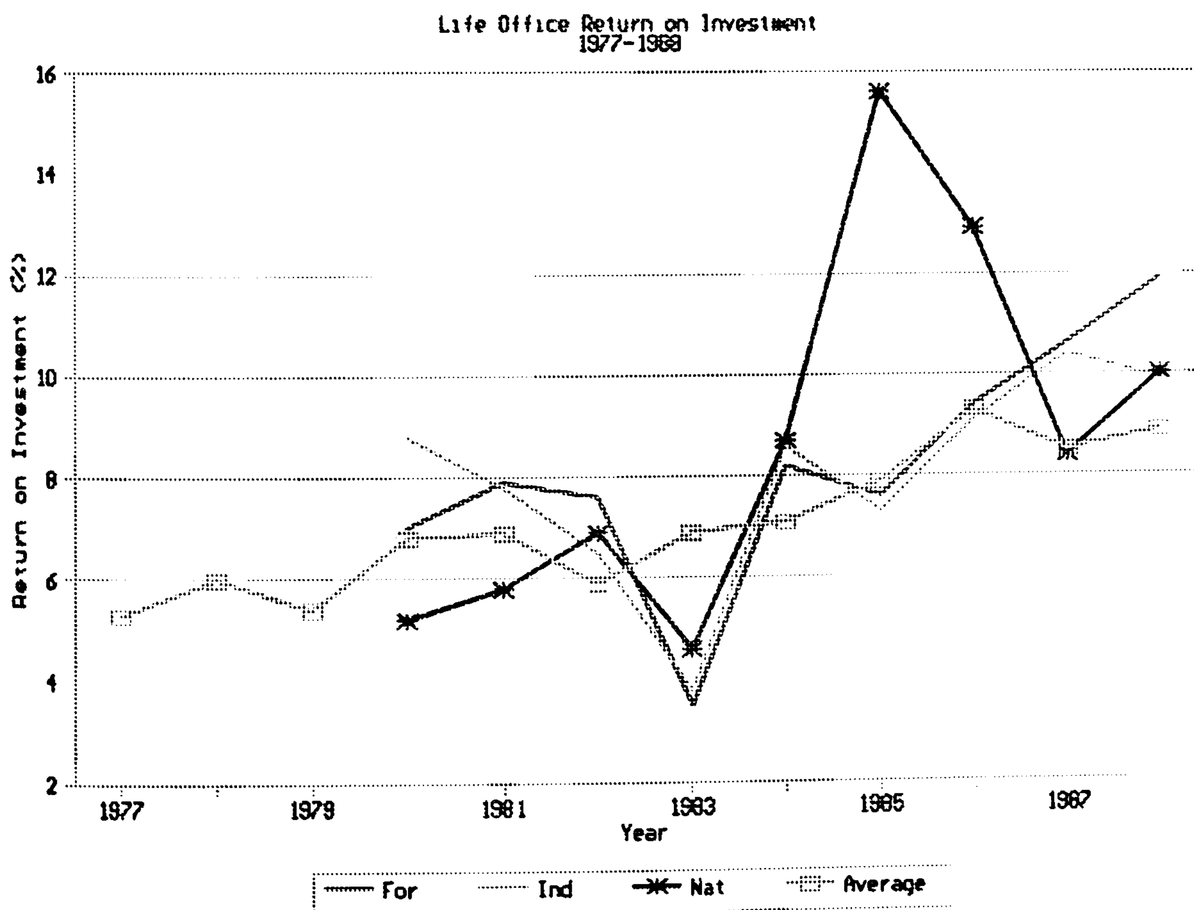


Figure 6L



6.4.4 Bonus Declarations

Life offices declare bonuses on their with-profits participating policies. These bonus payments are made to with-profits policyholders, much in the same way that dividends are distributed to shareholders, and are made from the surplus of the offices which is drawn from the income from invested assets. It is therefore expected that the bonus rate will be positively correlated with the rate of return on assets. When this occurs, the participating policyholders interests are being protected since they are participating in the profits of the life offices. A time series model was fitted to determine the nature of the relationship between the dependent variable BR (bonus rate) and ROA (return on invested assets). The form of the model was

$$BR = \beta_1 + \beta_2 ROA \qquad [8]$$

The dummy variables MIL, OIB, and $DEC59^{+4}$ were initially included in the model but dropped for lack of significance. It was expected that bonus declarations would be positively correlated with the return on invested assets. +

Table 6.34
Time Series Bonus Declaration
Regression Analysis 1977-1988

VARIABLES	BR
Constant	10.67
	(3.64)*
INV	-0.89
	(-2.18)*
S	1.88
R^2	25.50
Dw	2.03+
F	4.77~
LM[1]	0.50645^

* t-statistic significant at 5%
~ F value significant at 5%
+ Durbin Watson test applied at 1% level of significance
^LM test at 1 degree of freedom , 5% significance level

The results show that the rate of bonus declared by the life offices actually decreased with increases in return on invested assets (table 6.34). Since the rate of bonus declared does not appear to be dependent on the economic conditions specified, the implication is that there are other factors which determined the life offices policy on bonus declarations, such as, the level of operating profits, and expected future

expenses. Since precise information on these variables was unavailable, they could not be included in the model. Cross-sectional regression analyses of the relationship between these variables for the years 1981 and 1988 did not yield any significant results.

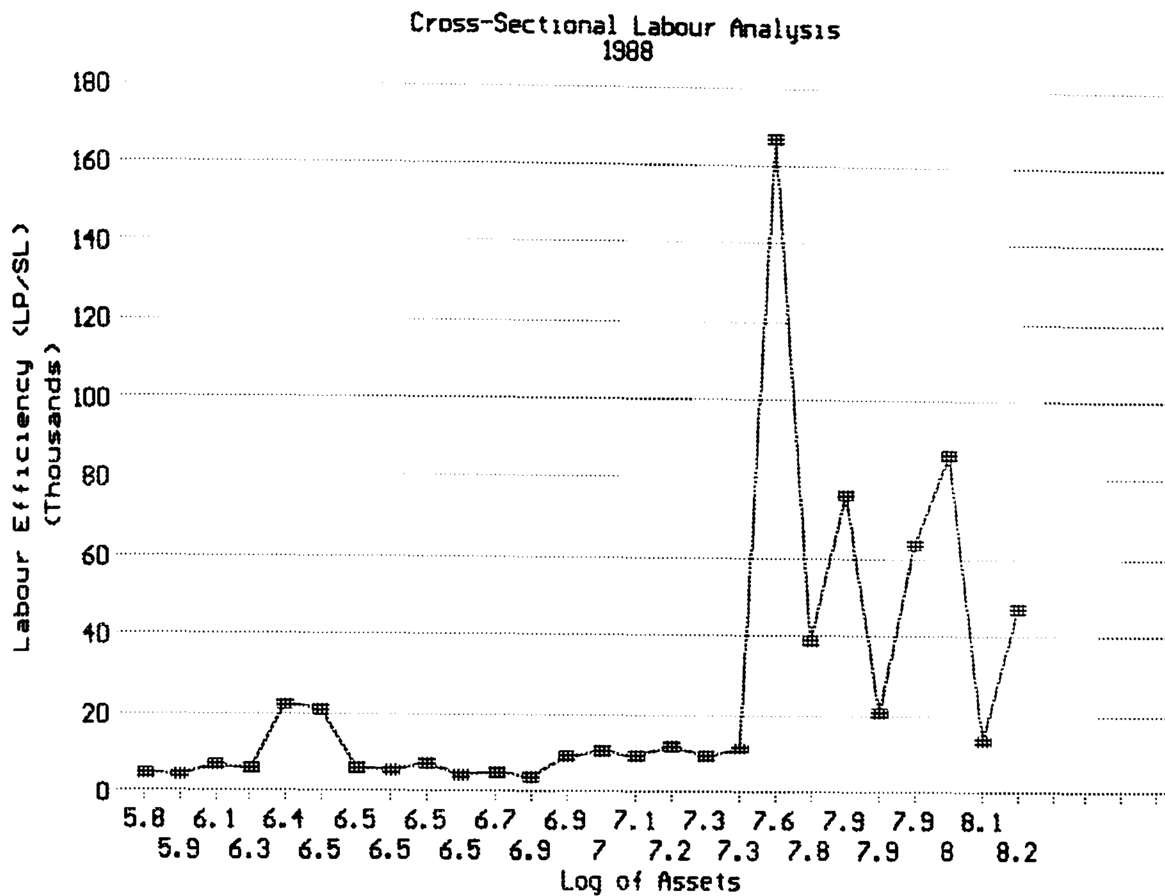
6.4.5 Labour Productivity

A measure of the relative efficiency of the life offices would be their efficiency with respect to the amounts of premium generated by an individual employee. Life premiums serve as a proxy for the output of the firm. Since the products of the offices are not homogenous, it would be expected that output (and as such productivity) would vary with the product mix of individual offices, as well as the proportion of the various policies in the company's portfolio. This information was however unavailable. The unavailablity of comprehensive labour force data precluded a cross-sectional study for 1981. An attempt was made to generate a regression model from 1988 data to investigate the nature of the relationship between labour productivity, the various types of company, the offices asset base and size of labour force. The results did not however yield meaningful results. Insufficient data precluded a time series analysis of the data.

In figure 6M the relationship between labour productivity (defined as LP/SL, the amount of total life premiums divided by the size of the labour force) and the logarithmic transformation of the size of total company assets (LogA) is displayed. Asset size has been employed as a measure of size of life office, as this variable is a better estimator of size of life office. The expectation was for labour productivity to increase with size of company if the labour force was efficient. The resultant graph yielded a curious result. It shows that as expected, there appears to be a direct relationship between labour productivity and asset size,[71] with the smaller companies

72. For the 1988 data asset size (Log A) and premium size (Log LP) were found to be highly correlated with a correlation coefficient of 0.88.

Figure 6M



being less labour efficient in comparison with the larger ones. From asset size 5.8 to 7.3 there was little variation in the labour efficiency indicator. However from asset size 7.6, there is a sharp change in the trend of the data. The labour efficiency indicator rises sharply and then falls again, though not to the level of the relatively smaller companies. There is a considerable variation in the values for 8 out of the biggest 10 life offices, so much so that it appears that the graph is displaying two different sets of data. The explanation for this may lie in the differences in the way in which the different categories of company report their data. It is also possible that the bigger companies are able to generate very large amounts of premium income with a relatively smaller work force. The obvious discontinuity however remains unexplained.

6.4.6 Retentions

One of the objectives of government regulation has been to increase the capacity of the life market by increasing the level of life office retentions, and keeping life

retentions however, has to be made with regard to the size and financial strength of individual offices. Thus, the level of capitalisation of the offices, as well as the amounts of reserves and size of life fund should be generally taken into consideration in making the retention decision.

The retention pattern of the Nigerian life offices was modelled in order to determine the variables that explain the level of retentions in the market. An attempt was made to model two different functions for the years 1981 and 1988 were modelled. However only one, the 1981 model yielded a meaningful result. The 1981 model was generated as follows:

$$RR1981 = \beta_1 + \beta_2\, CR_{t-1} + \beta_3\, B1 + \beta_4\, FOR + \beta_5\, NAT \qquad [9]$$

Since the view is taken in some industry circles that the level of capitalisation should be increased to raise market capacity by raising retention levels, a variable K, representing the level of paid up capital was initially specified in the model, but was dropped for lack of significance. A qualitative variable B2 which took the value 1 when the level of capital exceeded ₦1,000,000 and 0 otherwise also was not statistically significant. The variable CR_{t-1} defined as the level of capital and reserves in the previous year was included to take into account the effects of capitalisation and reserving. The lagged values of this variable was used in the model. The quantitative value for the size of the life fund was not included in the final regression as this was not a significant explanatory variable. However, a dummy variable B1 takes on the value 1 where the size of the life fund is greater than ₦20 million and 0 otherwise. The expectation is that the level of retentions RR, which is the amount of life premium income retained within the company (less reinsurance ceded plus reinsurances accepted) divided by total life premiums, should increase with the level of capital and reserves, magnitude of life fund, and with the size of the company. In other words, it is expected that the decisions on retention levels in a particular year should be made with regard to the level of capital and reserves of the life office in the previous years. It was expected that the positive relationship should be stronger in the case of life offices with big life funds (B1). A simple regression function was developed. The sample size was 16 rather than 18 firms, because the relevant data was unavailable for 2 firms. Table 6.35 shows that the model indicates that the level of capital and reserves was a significant factor determining life office retentions. When the variables for size of life fund, and type of ownership were introduced in a multiple regression, the results show in addition to the level of capital and reserves, a

multiple regression, the results show in addition to the level of capital and reserves, a big life fund was a determining factor in retention decisions. The sign of the coefficients for the variables FOR and NAT were negative as well as significant indicating that retention ratios were low, especially in the case of the foreign life offices.

Table 6.35
Cross-Sectional Retentions Regression Analysis
1981

YEAR VARIABLES	1981S RR81	1981M RR82
Constant	85.94 (27.32)*	90.05 (28.26)*
CR_{t-1}	1.05E-05 (3.03)*	1.03E-05 (3.13)*
B1		7.07 (2.04)**
$LogLp_{t-1}$		
FOR		-11.12 (-2.63)*
NAT		-7.09 (-2.14)*
S	5.74	4.99
R^2	33.80	49.90
F	9.17~	4.99~

*t-statistic significant at 5%
~F value significant at 5%
**t-statistic significant at 10%

Graphical representation (figure 6N) indicates some skewness (negative skewness). The implication is that there is some degree of bias in the estimators. However, the general trend appears to be that retention increases as the size of the capital and reserves increases.

A time series model in the form

$$RRTS = ß_1 + ß_2 \, LogLp_{t-2} + ß_3 \, DEC59^{+4} \qquad [10]$$

was estimated to examine the trend in retentions over time. The time series model contained one dummy variable $DEC59^{+4}$. The variables for level of capitalisation, economic prosperity and military period were initially included in the model but were later dropped due to lack of significance. The results indicate a negative time series

was the premiums in the previous year lagged by two periods to take into account the trend effects. This suggests that the life offices in times when a trend towards decreasing premium income was observed, increased their percentage of retentions probably in order to generate some working capital. Retentions were positively correlated with DEC56^{+4}, the period just following the implementation of the various regulatory rules (table 6.36 and figure 6O).

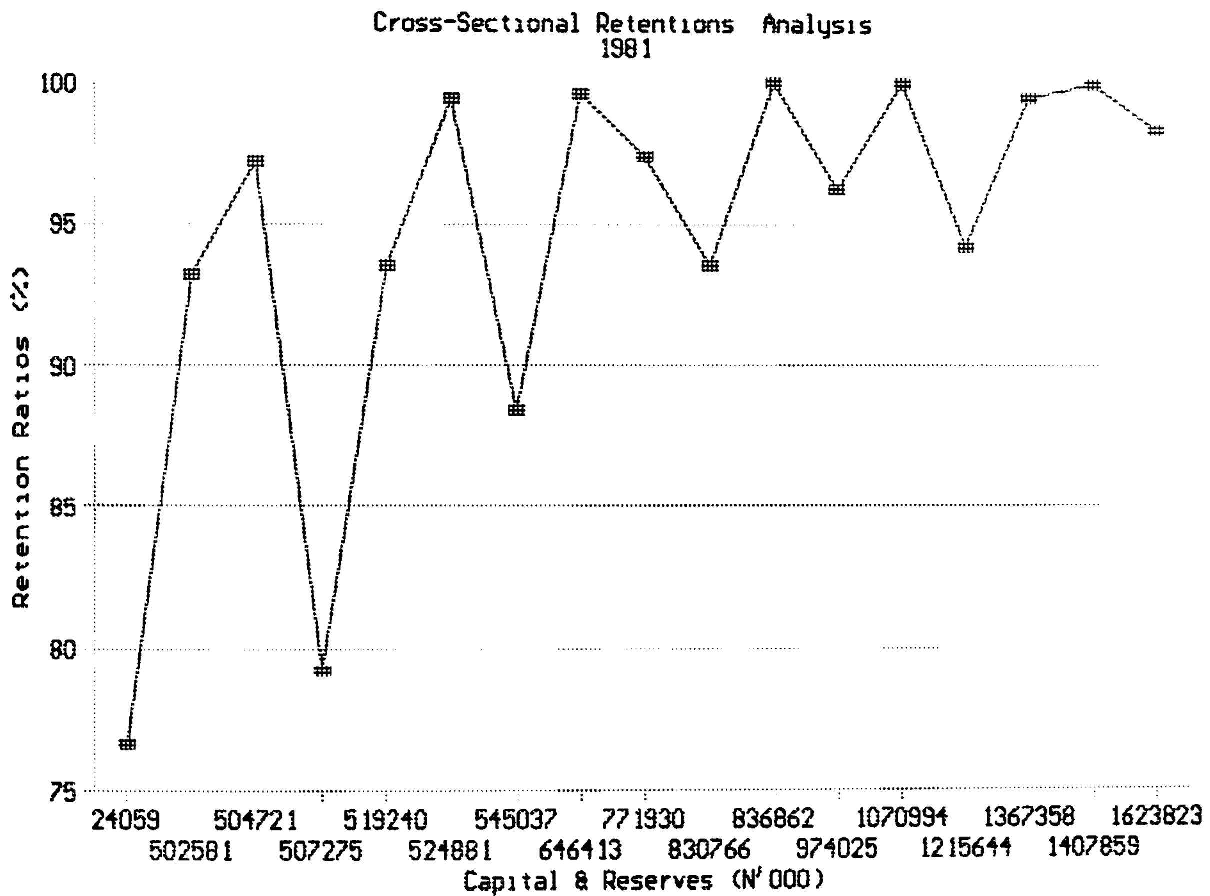
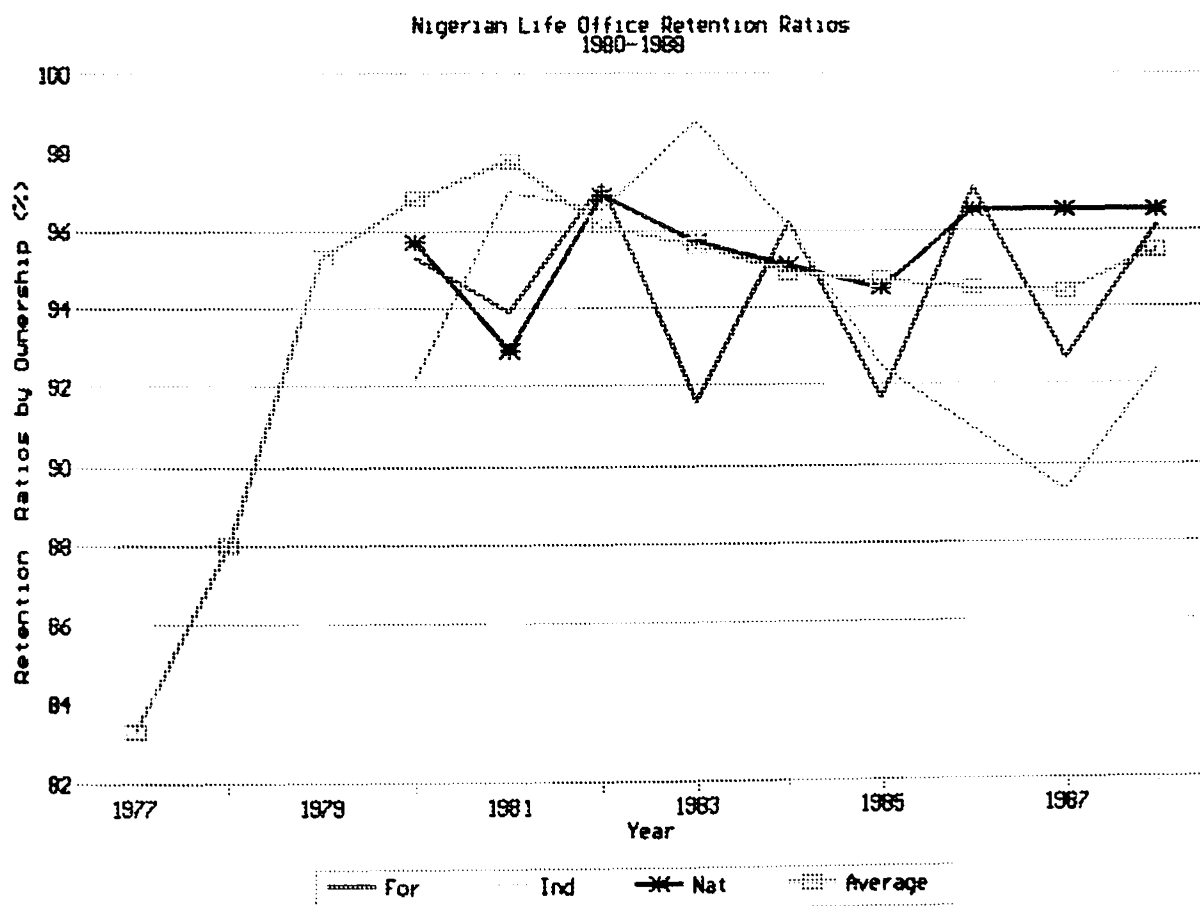


Table 6.36
Time Series Retention Ratios Regression Analysis 1977-1988

VARIABLES	RR
Constant	123.15
	(254.85)*
$LogLP_{t-2}$	-57.18
	(-46.59)*
$DEC59^{+4}$	0.86
	(75.19)*
S	0.04
R_2	99.90
Dw+	2.11
F	4289.99~
LM[1]	4.9775^
N[2]	2.180^^

*t-statistic significant at 5%
~F value significant at 5%
+Durbin Watson test applied at 1% significance level
^LM test at 1 degree of freedom, 10% significance level
^^ Normality test at 2 degrees of freedom

Figure 60



For the control sample, figure 6O shows that the total market retention ratios increased between 1977 and 1981 and have been declining slightly since then, although there was a slight increase between 1987 and 1988. Again on average the national offices retained more of their premiums (95.6%) than the foreign offices (94.6%), and their retention rates were more stable than that of the foreign offices.

Table 6.37
Nigerian Life Office Performance Ratios by Class of Ownership 1980-1988

Performance Indicator	FOR	IND	NAT	TOTAL	CONTROL SAMPLE
Expenses (%)					
AVG	37.2	36.5	33.5	35.9	35.7
STD	4.7	8.8	10.4	4.4	7.1
Claims (%)					
AVG	12.9	11.5	27.9	16.8	17.4
STD	2.0	5.3	9.6	4.2	5.7
ROA (%)					
AVG	8.2	8.0	8.7	7.6	8.1
STD	2.2	1.9	3.5	1.1	2.2
Retentions (%)					
AVG	94.6	93.9	95.6	95.6	94.7
STD	2.1	3.0	1.2	1.1	1.8
Assets (₦'million)					
AVG	2275.9	344.7	1435.8	5114.7	4056.4
STD	351.4	64.7	379.5		

Note: (1) AVG denotes mean value and STD denoted the standard deviation (2) ROA denotes return on invested assets.

SUMMARY

The objectives of Government regulation of the Nigerian life insurance market have been aimed at protecting the policyholders interest, strengthening the domestic insurance and reinsurance markets, and enabling the market to make significant contributions to the nation's economic development. A comparison of prior market structure and behavioural patterns in the Nigerian life market in two different periods (1960-1976; 1977-1988) leads to the following observations.

Market structure has not changed appreciably and the market remains highly concentrated. Although the implementation of domestication policies resulted in changes in ownership of some life offices, the effect has been merely to transfer market power from the foreign life offices to some of the national and joint venture companies. Entry into and exit from the industry declined over the period, although

there is some evidence of competition among the largest life offices. The evidence of the existence economies of scale in the time period following the implementation of regulatory rules and in recent times suggests that entry barriers have been supported by the existence of economies of scale.

The average results of life office performance indicators appear to suggest that the national life offices are leading the foreign life offices in terms of expenses, claims ratios and investment performance. However a close examination of the time series trends indicates that since 1985 foreign life offices expense ratios have been lower than those of the national companies. In addition to this, although the average expense ratios of the foreign offices were higher than those of the national life offices, this can be attributed to the higher salaries per employees paid in the foreign offices which appear to be justified by their higher labour productivity. Time series analysis indicates that in general, during the 1977-1988 period, there was no evidence for the existence of size economies in the market, with respect to management expenses, and the 1988 data show that labour productivity varies inversely with size of labour force. The 1988 cross-sectional data also indicate that most of the life offices (all the composites) were labour inefficient.

Since 1986 the foreign life offices return on assets ratios has been higher than that of the national and indigenous life offices. Total life office investments rose in real terms over the period with the foreign life offices investing more funds in various financial instruments than the national and indigenous offices. However, the life offices still kept a significant proportion of their funds in liquid assets and their bonus payments decreased with increasing investment performance.

Although the life market was the greatest contributor to total insurance industry premium income during the period from 1977-1988, the average growth rate in life premium income in real terms declined from 19.4% in the pre 1976 period to just 3.4% in the period from 1976-1988. Expenses and claims ratios were high during the period of military rule reflecting the structural adjustments to the economy at the time. The total life industry expense ratios were stable during the early 1980's, rose in the mid '80's, fell, and since 1987, appeared to be on the increase again. Although the total life market claims ratio rose steadily over the period, there is evidence that an appreciable proportion of the claims payments were in the form of payments for lapses and surrenders. A measure of total market asset growth was achieved but this also appears to be on the decline. Similarly there was, in general, a steady increase in

the level of total market return on invested assets with the suggestion of a slight decline since 1987. The level of real capital and reserves fell consistently over the period. Although the size of the life fund rose between 1977 and 1986, it's total contribution to economic development did not improve. The products sold and services offered do not appear to have changed significantly, and the credibility of insurance intermediaries has not improved over the years. In addition, the patterns of distribution of life insurance products remained basically the same. The demand for life insurance was positively correlated with the level of personal disposable income in the economy, however, its contribution to economic development remained marginal and has been on the decline since 1983.

Despite the fact that retention ratios in the life market have remained high, in real terms there has been a decline in retentions and by implication retention capacity. Life office retentions in real terms rose slightly over the period, with the highest increases in the period just after the implementation of regulatory rules, but by 1988 they were almost at 1977 levels. Size of company and a big life fund appeared to be the significant factors determining retention levels.

Thus the environment within which the life offices have been operating appears to have encouraged a market structure in which there is high concentration, significant barriers to entry and cost inefficiencies. This has serious implications for the performance of the life offices since high concentration invariably results in the misallocation of resources, increasing costs and poor economic performance. The results appear to suggest that the Governments policy goals vis a vis the insurance market have achieved mixed results. A comparison of the experience of the national and foreign life offices does not indicate that the national offices are superior in terms of their performance. There is imperfect competition in the market and the decline in capital and reserves and more recently the size of the life fund, is not in the policyholders interest. Despite policy efforts to stimulate and strengthen the market, growth in real terms has been marginal.

Chapter 7

Summary, Conclusions and Recommendations

7.1 Summary and Concluding Remarks

The economic and political developments in Nigeria indicate that the country has been economically and politically unstable. Economic conditions are difficult, the communication systems are inadequate and there is a lack of adequate infrastructure, features that are characteristic of developing country economies. In an attempt to stabilise the economy, various governments have formulated and attempted to implement various fiscal and monetary policy measures. The frequent changes in political leadership has led to inconsistencies in government policy over the years and this has contributed to inadequacies in financial policy and by implication the problems of the economic system. The regulation of the Nigerian insurance market has been in response to the presence of market inefficiency. However, because there was in general, in the past, no clearly defined policy specific to the insurance sector, legislative action has been reactive, rather than planned or anticipatory.

In recent times however, the Government has taken the view that the industry should be stimulated so as to be a potential generator of funds which are to be mobilised for the nation's economic development. In addition to this, a concern with the public interest has resulted in the Government's increasingly restrictive regulation of the insurance industry in general and the life insurance industry in particular. Consequently, the stated primary objectives of insurance regulation in the country have been focused on the protection of the public (consumer) interest and the development of a strong domestic insurance and reinsurance market, within the nation's developmental framework. This has led to two categories of insurance legislation: the industry specific rules which are primarily focused on the insurance industry, and the general economic policy which affect all sectors of the economy.

As a result of the implementation of various regulatory rules, regulatory philosophy has shifted over the years from one of relative freedom of operation in the market to a system of close supervision of insurance business. Restrictions have been placed on

the insurance market on a services and establishments basis, so that the nature of legislation has been protectionist. The Government has actively participated in the life insurance industry not only through regulatory activity, but through the establishment and operation of national insurance companies. The activities of foreign insurers has been restricted by the acquisition of equity in these companies by private and public parties.

However, the effectiveness of the industry specific rules has been hampered by, among other things, the inability of the Insurance Department to enforce the rules, and non-compliance with various aspects of the regulatory provisions. The Department is professionally understaffed and lacks the financial resources to carry out its responsibilities. Apart from this the Insurance Department is not an independent agency, and under military administrations especially, it does not appear to have a significant degree of decision making power. The actual determination of public policy with respect to the insurance industry appears to have been done by the political elite with relatively little influence from the civil service.

In the 1960's, powerful (foreign) interest groups in the industry were able to influence legislative activity to the extent that the regulations in force were largely ineffective and mainly in the producer interest. In more recent times, the evidence suggests that the insurance industry has been unable to influence the nature and scope of regulatory policy and there is no evidence, at the present time, of regulatory capture.

However, the intent of regulation and regulatory rules is one thing and the reality of the effect of the rules is another. Although the focus of regulatory effort is supposed to be a concern with the public and national economic interest, the changes in life industry structure, conduct and performance indicate that this has not been achieved. The growth of the life market in real terms has declined and the level of life industry capital and real reserves has, in real terms, been declining raising questions of life insurer solvency. Although the size of the total life industry life fund increased during the late 70's and early 80's, since the mid eighties, this has in real terms, been on the decline. The contribution of the life insurance market to GDP has not increased over the years. In addition to this, there is insufficient evidence to establish the success of the policy measures taken by the Government to improve the balance of payments position by reducing the amount of foreign currency reinsurance outflows to the western reinsurance markets. In comparative terms, the national life offices, which were established to improve market efficiency, have not established a clear-cut superiority over the foreign offices, although in terms of claims they appear to have achieved a higher degree of operational efficiency. However, in terms of the

generation of funds invested in the economy and labour efficiency, the foreign offices have been performing better than the national life offices. The average performance of the indigenous (domestic) life offices has been disappointing. Thus, in the Nigerian case, the implementation of restrictive protectionist policies in the life insurance market has not achieved the stated policy objectives. The problem however, is not with the principle of protectionism per se. The experience of some developing economies[1] has shown that such measures can be beneficial to the development of such markets. In the Nigerian situation, the failure of this policy to achieve stated goals has been as a result of, among other things, the inherent problems in economic structure and management and ineffective implementation and supervision. In addition to this, protectionism has been seen as the panacea for the nation's economic troubles and protectionist rules have been implemented without regard to the prevailing and long-term economic situation. The rules have to be formulated and applied in line with the economic framework and in some areas limited protectionist policies may have to be put in place to achieve the long-run desired results. There are some lessons to be learnt. In the past, the blanket application of a restrictive regime has resulted in the situation where the Government has, in recent times, been compelled to back-track on protectionist policies in some other sectors of the economy.[2]

7.2 Recommendations

In an attempt to improve insurance market efficiency, the Government is believed to be taking steps to promulgate and implement a new insurance decree. Although the provisions of the new decree were not known at the time of writing, there was speculation that the capital licensing requirement for the establishment of new life insurance companies was to be raised to ₦5 million to discourage the entry of inefficient insurers into the market. It was reported that industry sources wanted the capital base raised to ₦10 million.[3]

However, although an increase in the capital base could possibly discourage the entry of the so called inefficient insurers into the market, this would not resolve the

1. For example, Brazil, Korea and Tanzania (See section 3.4).

2. See chapter four, section 4.2.3, pp.96-97.

3. See for example, The Daily Champion, Wednesday May 22 1991,p.9; The Daily Times, Wednesday May 22, 1991,p.27 and The Guardian on Sunday, May 12 1991,p.A3.

problems of market inefficiency and the slow growth of the life market. Indeed the modelling of life market retentions in this study revealed that the level of capitalisation is not a significant determinant of life office retentions, and as such an increase in the level of capitalisation is unlikely to increase the retention capacity of the market. The evidence from this study of the Nigerian life insurance market indicates that effective policy implementation has been hampered by, among other things, the general economic situation and lax supervision. Various problems need to be addressed, at the life industry level and on a general economic level, and this leads to the following recommendations.

(1) The Government should, if it is committed to ensuring the growth and efficiency of the life insurance industry, review and amend some of the regulatory rules affecting the industry. Of particular significance are:

(a) The provisions in the 1976 decree relating to the valuation of the assets and liabilities of the life offices.[4] The way the rules stand, the life offices make valuations based on any valuation method which is to their liking. Although an actuarial valuation would be needed to assess the full impact of this, the fact that over the years the value of reserves (and more recently the life fund) have declined is evidence of the increasingly precarious position of the life offices in terms of future solvency. Apart from this, the instability of the financial market makes the estimation of future interest rates difficult and there is a danger that in the future a number of life offices could eventually collapse. Indeed, given the inadequacies of the supervisory system, there is a possibility that a number of companies could be operating at near insolvency levels. This should be a cause for concern and the recent experience of some big life insurers in some western markets has shown that this is a real danger.[5]

(b) In addition to this, the restrictions on life office investment activity[6] need to be reviewed within the framework of the economy. The imposition of a maximum ceiling on investment in private shares and land, and a minimum level of investments in government assets may not be achieving the national interest. The life offices have, within the restrictive measures, been achieving a measure of success in terms of investments returns. The life market (and indeed the

4. See see chapter five, section 5.3.2.4, pp.130 & 132.

5. See for example, Kopcke and Randall (1991), Wright (1991).

6. See for example, chapter five, section 5.3.2.4, p.130.

whole insurance sector) cannot continue to subsidise the Government by this indirect form of taxation. It is in the policyholders interest (and by implication the larger economic interest) if the life offices are allowed greater freedom in designing investment strategies which will result in higher returns on invested assets. If the improved performance of life offices leads to a better service to policyholders in terms of product quality, and this increases consumer confidence and investment in the life market, then ultimately this will be in the national economic interest since increased savings will ultimately be employed in economic development.

(c) Under the provisions of the 1988 Privatisation and Commercialisation Decree[7] the Government took the steps to divest itself of all of its equity in insurance companies in which it had joint foreign and/or indigenous participation. The national companies however, were not subject to privatisation. The Government simply "commercialised" these companies. This meant that these companies would still continue to be fully owned by the Government, but would be expected to operate without any financial support from the Government. The companies would be left to raise capital from non-government sources. The Government, in order to make the measures it has been taking to deregulate the economy meaningful in the context of the life industry should divest itself of some of its equity in all the national companies. The experience over the years indicates that the national life offices have not achieved the status of "market leaders" for which they were primarily established, and this could be due to their having to operate within the generally inefficient bureaucratic framework of the Government. The Government's continued regulation of the industry in the form of extensive participation by the national companies has been costly in terms of resource allocation. Although it would be difficult to measure the full extent of the financial resources committed to the establishment and maintenance of these companies, the fact that they are not fulfilling their established purpose indicates that the costs outweigh any associated benefits. The Government has admitted the fact that it has failed to cover the costs of operation in it's public sector companies.[8] In order to stimulate competition within the entire market, the partial privatisation provisions of the Privatisation decree should be extended to the national insurance companies and foreign and indigenous equity investment in these companies should be encouraged. The Government should withdraw from its present intensive participation in the

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7. Section chapter four, section 4.2.3, p.96.

8. See section 4.2.3, p.96.

market and channel it's resources towards maintaining an effective regulatory mechanism.

(d) Size, and not ownership appears to be one of the principle determinants of life insurer efficiency. This is the case with respect to economies of size, labour efficiency and to some extent, retentions. This leads to the suggestion that the Government, in developing and establishing regulatory rules should aim to encourage life insurance market consolidation. There is no need for the Government to continue it's extensive participation because the experience of the national companies (on the basis of the objectives for which they were established) does not justify their continued participation.

(2) The Insurance Department cannot be expected to fulfil it's supervisory functions if it is continuously subject to financial and human resources handicaps. The Department cannot effectively perform it's functions (especially with respect to monitoring solvency and the approval of life policy forms and rates) without the requisite professional staff. Unless the Department is adequately funded and modern systems of record keeping installed, it will continue to be ineffective. The present civil service salary structure is insufficient to attract and keep the specialised personnel needed to monitor insurance company solvency among other things, and a review is overdue.

(3) The Government's decision to localise the reinsurance activities of the life market was supposedly taken in the national interest. However, there appears to be a conflict with the national and policyholder interest. Although this decision, it is said, will result in the retention of more life funds within the market, which would possibly be in the national interest (if these funds are not expended on technical agreements with western reinsurers) it is not clear whether and how this will ultimately improve the quality of service to the policyholder. The fact that there is insufficient expertise in the area of life reinsurance is not disputed, and inefficiencies in this area will simply, among other things, raise the cost of life insurance to policyholders. Thus the Government's decision to was apparently based primarily on political considerations, and was precipitate given the present state of the insurance market.

(4) The relationship between a viral economy and a viral life insurance industry has been established. In the case of the Nigerian life market, empirical analysis has established that about 80% of life office retention behaviour can be explained

by the total premium income of the life offices. The implication is clear-the life market has to generate more output in order to increase market capacity. However, the life market operates within the broader macro-environment and as long as the economic situation in the economy remains at the currently depressed levels, it will be difficult to stimulate and sustain effective growth in the industry. It is difficult to foresee, in the long-term, any significant improvement in life industry growth. The fact that over 70% of the life insurance sold is in the form of group life insurance is an indication of the seriousness of the situation. Unless people are "compelled" to purchase life policies through group plans at work, they will in general not utilise this form of saving and investment.

It has to be recognised that the various economic measures taken by the Government will impact on the industry, and a concerted effort has to be made to coordinate and integrate these with general economic measures to sustain a viable life market. It is not sufficient for the Government to state that its regulatory objectives are premised on a concern with the consumer and public interest. The reality of the situation is otherwise. If the Government does not demonstrate a real commitment to these goals then regulation of the industry will continue to be mere ritual.

(5) In order to ensure the industry's continuing survival, the life offices have to develop ways to obtain an increasing part of potential policyholder income. This means an emphasis on innovative activity and a willingness to fund research into the industry.

The above recommendations as regards the (de)regulation of the life industry have been made with a view to stimulating allocative efficiency and enhancing the innovative and technological progressiveness of the market. The level of total market life premium income needs to be increased so that this sector of the economy could serve as a source through which funds could be effectively channelled into the capital market. It has to be recognised however that the recommendations made might have some possibly perverse effects on the life insurance and capital markets. For example, deregulation of investment activity may result in a reduction in the amount of funds that are invested in government assets, which could reduce the amount of capital funds available to the government.

In addition to this, life insurance market consolidation, while increasing general market efficiency might tend towards increasing monopoly power. However, it is expected that the welfare effects to be achieved from implementing these measures will outweigh any potentially negative effects. As an illustration, in the case of investment activity, although investment in the public sector might be considerably reduced, the expected increase in private sector investments is expected to be more than compensatory and to be beneficial to the life market as a whole.

7.3 Suggestions for Further Research

The conclusions made in this study are based on the results of the theoretical and empirical analysis of available data. However, it has to be recognised that these are subject to certain limitations in the data. It cannot be assumed that the variables employed in the empirical analysis have been measured without any errors. Error free measurement of variables is an ideal which is unfortunately not met in practice. in the case of the Nigerian life market data, there are limitations with respect to :

(1) The non-availability of requisite data

(2) Incomplete data across the spectrum of companies, that is, non-response errors

(3) Inconsistencies across the various data sources, that is, reporting errors.

These are mainly due to the problems with the collection and compilation of data on insurance market operations. The assumption has been made that the problems of measurement detailed above are of sufficiently small magnitude to enable the estimations based on the data to be acceptable. The tests for normality, auto-correlation, multicollinearity and heteroscedasticity that have been applied to the data suggest that these deficiencies are not a major problem.

This study has attempted to throw some light on the interrelationships between regulation, structure, behaviour and performance in the Nigerian life market. The life insurance market is however, strictly speaking, not homogenous across product lines and separate individual studies of the individual life and group life markets would probably increase the understanding of the market.

Although regulatory effects in the non-life market have been studied, most, if not all, of this has been theoretical; and empirical analysis in this area will be needed to obtain a wider picture of the dynamics of the insurance industry as a whole.

The impact of strategy upon operational profitability is also of utmost importance in any industry, and more especially in the life market where market share leadership predominates. A detailed study of the effects of market share and concentration on profitability is therefore essential to determining the efficiency or inefficiency of the insurance market. In addition to this there remains much work to be done concerning the nature of the oligopolistic bargain in the life market, how this is influenced by market structure and how this has affected industry performance.

The effects of the localisation policies in respect of the reinsurance transaction is another area for future study. Since the Government has repeatedly placed emphasis on it's belief that this course of action is in the economic and policyholder interest, it is necessary to evaluate these effects, to arrive at a definite conclusion.

In addition to this, an empirical analysis of the determinants of insurance company investment behaviour in the life and non-life markets is needed.

The above presupposes the existence of a reliable and accessible database from which relevant data can be extracted in order to examine these issues. This at the time of writing is unfortunately, lacking. Although the Nigerian Insurance Association should be commended for independently attempting to do this, the information source is still seriously lacking in the necessary and requisite micro-company data which are so important in these types of analyses. There is obviously still a lot of work to be done in this area.

APPENDICES

Appendix A: Tables

Table A1
Nigerian Stock Exchange Transactions 1960-1989
(N'million)

Year	Government Securities Value	%	Industrial Securities Value	%	Total Value
1961	1.4	(94.0)	0.09	(6.0)	1.49
1962	4.2	(92.7)	0.33	(7.3)	4.52
1963	9.7	(93.8)	0.64	(6.2)	10.34
1964	11.8	(84.3)	2.20	(15.7)	14.0
1965	14.4	(90.6)	1.50	(9.4)	15.99
1966	15.2	(92.7)	1.20	(7.3)	16.40
1967	12.1	(97.6)	0.30	(2.4)	12.40
1968	12.6	(98.5)	0.21	(1.6)	12.81
1969	16.2	(98.9)	0.18	(1.1)	16.38
1970	16.4	(98.6)	0.24	(1.4)	16.64
1971	16.3	(90.1)	1.80	(9.9)	18.10
1972	26.2	(96.4)	0.98	(3.6)	27.18
1973	91.9	(99.4)	0.53	(0.6)	92.43
1974	49.4	(97.4)	1.30	(2.6)	50.70
1975	62.8	(98.6)	0.90	(1.4)	663.70
1976	111.3	(99.5)	0.56	(0.5)	111.86
1977	178.8	(99.3)	1.22	(0.7)	180.02
1978	187.1	(98.8)	2.40	(1.2)	189.50
1979	257.5	(98.3)	4.40	(1.7)	261.90
1980	503.4	(98.3)	8.60	(1.7)	512.00
1981	324.0	(98.2)	6.10	(1.8)	332.10
1982	206.5	(96.1)	8.30	(3.9)	214.80
1983	384.7	(96.7)	13.00	(3.3)	397.70
1984	402.8	(96.3)	15.40	(3.7)	418.20
1985	296.0	(92.7)	23.60	(7.3)	319.60
1986	470.3	(95.5)	23.70	(4.5)	492.70
1987	307.7	(88.4)	40.10	(11.6)	348.00
1988	104.9	(76.3)	32.70	(23.7)	137.60
1989	462.0	(88.5)	59.60	(11.5)	521.60

Source: Compiled from data supplied by the Nigerian Securities Exchange, Lagos

Table A2
Nigerian Stock Exchange Transactions 1960-1989

Year	Government Securities Number	%	Industrial Securities Number	%	Total Number
1961	92	(27.5)	242	(72.5)	334
1962	175	(25.2)	520	(74.8)	695
1963	296	(41.6)	415	(58.4)	711
1964	404	(41.0)	581	(59.0)	985
1965	391	(38.40	627	(61.6)	1018
1966	501	(45.7)	595	(54.3)	1096
1967	336	(44.0)	427	(56.0)	768
1968	286	(44.3)	360	(55.7)	646
1969	307	(55.5)	246	(52.2)	553
1970	303	(47.8)	331	(52.2)	634
1971	204	(21.4)	748	(78.6)	952
1972	258	(28.7)	640	(71.3)	898
1973	232	(34.4)	537	(65.6)	819
1974	256	(8.4)	2807	(91.6)	3063
1975	193	(27.8)	501	(72.2)	694
1976	321	(31.6)	696	(68.4)	1017
1977	337	(20.4)	1314	(79.6)	1651
1978	243	(9.8)	2230	(90.2)	2473
1979	124	(3.8)	3099	(96.1)	3223
1980	211	(3.0)	6843	(97.0)	7054
1981	117	(1.1)	10101	(98.9)	10218
1982	185	(2.0)	9218	(98.0)	9403
1983	291	(2.4)	11625	(97.6)	11916
1984	195	(1.1)	17170	(98.9)	17365
1985	320	(1.4)	23060	(98.6)	23380
1986	271	(0.7)	26404	(99.3)	26583
1987	230	(1.2)	19353	(8.8)	19583
1988	88	(0.5)	17928	(99.5)	18016
1989	150	(0.7)	22346	(99.3)	22496

Source: As in Table AI

Table A3
Interest Rate Structure and Inflation in Nigeria 1960-1987

Year Rate	Discount Rate	Deposit Rate	Lending Rate	Inflation Rate	Real Deposit Rate
	(1)	(2)	(3)	(4)	(2)-(4)
1961	5.50	3.00	8.00	6.40	-3.40
1962	4.50	3.00	7.00	5.30	-2.30
1963	4.00	3.00	7.00	-2.70	5.70
1964	5.00	3.00	7.50	0.80	2.20
1965	5.00	3.50	7.50	4.10	-0.60
1966	5.00	3.50	7.50	9.70	-6.20
1967	5.00	3.50	7.50	-3.70	7.20
1968	4.50	3.00	7.00	-0.50	3.50
1969	4.50	3.00	7.00	0.20	2.80
1970	4.50	3.00	7.00	13.70	-10.70
1971	4.50	3.00	7.00	16.10	-13.10
1972	4.50	3.00	7.00	2.70	0.34
1973	4.50	3.00	7.00	5.70	-2.70
1974	4.50	3.00	7.00	12.50	-9.50
1975	3.50	3.50	6.25	33.60	-30.10
1976	3.50	2.67	6.50	22.00	-19.33
1977	4.00	2.83	6.00	21.40	-18.57
1978	5.00	4.15	6.75	21.70	-17.55
1979	5.00	4.47	7.79	11.70	-7.23
1980	6.00	5.27	8.43	10.00	-4.73
1981	6.00	5.72	8.92	20.80	-15.08
1982	8.00	7.60	9.54	7.70	-0.10
1983	8.00	7.41	9.98	23.20	-15.79
1984	10.00	8.25	10.24	39.60	-31.35
1985	10.00	9.12	9.43	5.50	3.62
1986	10.00	9.24	9.50	5.40	4.10
1987	10.00	13.09	13.96	10.20	3.76

Source: Compiled from data from the IMF International Statistics Yearbook 1991, and the IMF Financial Statistics. 1961-1969 Deposit and Lending rate figures obtained from Ikhide 1990 in the Nigerian Financial Review 1990,p.44

Table A4
Yields on Government Stock

9.75	FRN	22nd	DS	1992
9.75	FRN	22nd	DS	1995
6.00	FRN	15th	DS	2001
6.00	FRN	8th	DS	1996
6.00	FRN	12th	DS	1999
6.00	FRN	9th	DS	1997
6.00	FRN	3rd	DS	1990
6.00	FRN	5th	DS	1993
6.00	FRN	2nd	DS	1989
5.00	FRN	6th	DS	1985
5.75	FRN	1st	DS	1988
5.75	FRN	4th	DS	1987
6.00	FRN	4th	DS	1992
6.00	FRN	16th	DS	2002

Source: The Business Times, January 23, 1984
Note: FRN denotes Federal Republic of Nigeria, DS, Development Stock

Table A5
Yields on Selected Industrial Stock

Ordinary Shares	**1980**	**1985**	**1991**
Financial	%	%	%
Union Bank	12.5	15	24.8
Manufacturing			
Cadbury	40.0	24.2	50.0
Commercial			
UTC	20.0	11.0	20.0
Pharmaceutical			
Glaxo Nig.Ltd	30.9	13.0	-
Petroleum			
Total	33.3	45.7	74.0
Construction			
Julius Berger	19.6	14.2	50.0

Source: Returns compiled from (1) 1980 figures, Business Times, June 24 1980, (2) 1985, Business Times, January 4 1985 (3) 1991, The Nigerian Stock Exchange Daily Official List, 4th October 1991
Notes: Yields on shares calculated as follows: Total Dividend/Nominal Value of share %

Table A6
Insurance Contribution to GDP
1973-1986

Year	GDP (1)	Insurance (3)	Non-Life/Life % (3)
1973/74	11224	0.16	0.11/0.05
1974/75	18652	0.13	0.10/0.03
1975/76	21475	0.19	0.16/0.03
1976/77	27318	0.22	0.18/0.04
1977/78	32052	0.25	0.21/0.04
1978/79	33360	0.35	0.29/0.26
1979/80	39939	0.41	0.33/0.08
1980	43280	0.45	0.36/0.09
1981	43450	0.52	0.40/0.12
1982	60483	0.42	0.31/0.12
1983	63293	0.31	0.20/0.12
1984	69950	0.25	0.15/0.10
1985	78776	0.18	0.11/0.07
1986	79740	0.15	0.09/0.06

Source:(1) GDP figures in ₦'000, 1973-1981, insurance contribution to GDP, obtained from Nigerian Gross Domestic Product and Allied Macro Aggregates: 1973/74-81, Vol.1 No.1, April 1992, Federal Office of Statistics, Lagos (2) GDP figures 1982-1987 Annual Abstract of Statistics, Lagos, 1986

Notes: (1) GDP figures at 1984 constant factor cost (2) Percentage contribution of life/non-life markets to total GDP estimated as follows: Direct Premiums (Life)/Direct Premiums (non-life) x Total percentage insurance contribution to GDP

Table A7
Growth in Retentions of Nigerian Life Offices
1977-1988 (₦'000)

Year	Retentions Nominal	Retentions Real	Growth Nominal	Growth Real	RR %
			1985=100		
1977	45,209	1,113			90.8
1978	54,335	1,124	20.2	1.0	97.5
1979	63,305	1,159	20.2	3.1	91.6
1980	87,374	1,386	33.8	19.6	96.8
1981	113,050	1,645	29.4	18.6	97.8
1982	112,634	1,604	-0.4	-2.5	96.1
1983	134,631	1,641	19.5	2.3	95.6
1984	127,348	1,323	-5.4	-19.4	94.9
1985	132,552	1,325	4.1	0.13	94.7
1986	174,889	1,786	31.2	34.8	94.5
1987	168,164	1,147	-3.8	-35.8	94.4
1988	198,560	1,116	18.1	-2.7	95.5

Note:(1) Retention figures obtained from Insurance Department, Lagos (2) Nominal figures have been deflated (3) RR denotes retention ratio.

Table A8
Expense Ratios By Ownership
1980-1988

Year	FOR	IND	NAT	MARKET
1980	40.1	35.3	28.5	34.5
1981	34.5	23.7	18.9	32.9
1982	47.7	30.4	27.9	35.3
1983	30.8	35.1	25.7	34.5
1984	39.5	30.8	27.5	31.8
1985	34.9	53.1	38.0	46.1
1986	33.9	41.8	54.0	38.7
1987	34.3	30.7	34.5	29.7
1988	39.1	47.4	46.1	39.8
AVG	37.2	36.5	33.5	35.9
STD	4.7	8.8	10.4	4.4
AVGS	7 1			
STDS	35.8			

Note: AVG denotes average, STD standard deviation, STDS standard deviation of the control sample, and AVGS average of the control sample.

Table A9
Nigerian Life Office Claims Ratios by Ownership 1980-1988

Year	FOR	IND	NAT	MARKET
1980	9.8	5.4	17.3	11.3
1981	9.9	5.9	15.4	10.8
1982	13.8	6.9	19.7	12.9
1983	12.5	8.5	23.1	15.2
1984	14.7	8.1	29.7	18.0
1985	14.2	19.8	45.9	22.1
1986	13.9	18.6	38.1	20.8
1987	15.9	15.4	33.6	21.6
1988	11.1	14.5	28.2	18.7
AVG	12.9	11.5	27.9	16.8
STD	2.0	5.3	9.6	4.2
AVGS	17.4			
STDS	5.6			

Table A10
Nigerian Life Office Investment Performance by Ownership 1980-1988

Year	FOR	IND	NAT	MARKET
1980	7.0	8.8	5.2	6.8
1981	7.9	7.8	5.8	6.9
1982	7.6	6.5	6.9	5.9
1983	3.5	3.8	4.6	6.9
1984	8.2	8.6	8.7	7.1
1985	7.6	7.3	15.6	7.9
1986	9.4	9.1	12.9	9.3
1987	10.6	10.4	8.4	8.5
1988	11.9	9.9	10.0	8.9
AVG	8.2	8.0	8.7	7.6
STD	2.2	1.9	3.5	1.2
AVGS	8.1			
STDS	2.2			

Table A11
Nigerian Life Office Investments by Ownership 1980-1988 (₦'000)

Year	FOR	IND	NAT	MARKET
1980	1758	246	1340	3739
1981	2109	415	1646	4403
1982	2444	317	1828	6273
1983*	2304	316.6	1491	5214
1984	2164	316	1154	4928
1985	2720	371	1263	5608
1986	2940	433	1569	6410
1987	1966	266	1998	4841
1988	2078	422	634	4617
AVG	2275.9	344.7	1435.9	
STD	351.4	64.7	379.5	

Note: 1983 figures estimated by extrapolation

Table A12
Nigerian Life Office Retention Ratios by Ownership 1980-1988

Year	FOR	IND	NAT	MARKET
1980	95.3	92.2	95.7	96.8
1981	93.9	97.0	92.9	97.8
1982	97.2	96.5	96.9	96.1
1983	91.6	98.8	95.7	95.6
1984	96.2	96.1	95.1	94.9
1985	91.7	92.5	94.5	94.7
1986	97.1	90.9	96.5	94.5
1987	92.7	89.3	96.5	94.4
1988	96.1	92.4	96.5	95.5
AVG	94.6	93.9	95.6	95.6
STD	2.1	3.0	1.2	1.1
AVGS	94.7			
STDS	1.8			

Table A13
Definitions of Variables Employed in Regression Analyses

VARIABLES	DEFINITIONS
Ownership	
**FOR	Foreign Life Offices
**NAT	National Life Offices
Structure	
**COMP	Composite Life Offices
Size	
LP	Life Premium Income
LogLP	Log of Life Premium Income
1/LogLP	Reciprocal Log Life Premium Income
1/P	Reciprocal Life Premium Income
SL	Size of Labour Force
A/SL	Total Assets per Size of Labour Force
*LP/SL	Labour Efficiency
LogA	Log of Assets
CR_{t-1}	Capital & Reserves in year t-1
**B1	Life Fund in excess of ₦20million
Financial	
NP/LP	New Life Business (% of Life Premiums)
GP_{t-1}	Goup Life Insurance in Force in year t-1
NB_{t-1}	New Businesss Underwritten in year t-1
LR_{t-1}	Lapse Ratio in year t-1
GS/TA	Poportion of Total Assets in Govt Stock
BS/TA	Poportion of Total Assets in Private stock
*ROA	Return on Invested Assets
*AC	Average Cost Ratio
*OE	Operating Costs Ratio
*ME	Management Expense Ratio
*Claims	Claims Ratio
*RR	Retention Ratio
Regulatory Periods	
**MIL	Military Administration
**OIB	Oil Economy
**DEC59^{+4}	Regulatory Lag Period

*Denotes independent variables
**Denotes dummy variables

Appendix B: Life Managers Interview Schedule

Interview Guide: Life Managers

Section A: Introductory

(Q1) Do you think that the insurance industry in Nigeria is heavily regulated or not?

(Q2) What about the life insurance industry?

(Q3) What is the basis for your opinion (why is that?)

(Q4) Would you like to see more or less regulation of life insurance in this country?

Section B: Market Structure

(Q1) Could you give me an idea of the structure of the life insurance industry in this country?

(Q2) Has this structure had any effect on the market?

(Q3) In what way?

(Q4) What in your opinion are the main barriers to entry into the life insurance industry? The general industry?

Section C: Market Behaviour

Product

(Q1) What kinds of life insurance policies does your company sell?

(Q2) What is the most popular policy underwritten? Least popular? Why is that?

** Ask for supporting data, that is, proportion of annuities,

single premium policies, endowments, whole of life assurance e.t.c

(Q3) In what way would you say regulation has had an impact if any, on your rating/pricing of life policies?

Intermediaries

(Q1) What kinds of intermediaries do you utilise in the distribution of life insurance?

(Q2) Which category would you say have been the most effective?

(Q3) Could you give an estimate of the number of intermediaries your company employs?

(Q4) What sort of problems do they encounter?

(Q5) Would you like to see more or less regulation of the activities of insurance intermediaries in the market?

Investments

(Q1) What is your opinion of the regulatory provisions regarding investments?

(Q2) Why is that?

Section D: Public Policy

(Q1) Do you feel that the Government consults with the industry before regulatory rules are introduced?

(Q2) If this is the case, to what extent do you feel that the government takes the advice of the industry?

(Q3) Do you find it relatively easy to comply with regulatory

rules such as solvency requirements

filing business returns

actuarial valuation of assets and liabilities

contribution to the special provision fund? e.t.c

(Q4) Which aspect(s) of regulatory policy are you most satisfied with? Dissatisfied with?

Section E: Claims

(Q1) What particular aspects of claims settlement is the most problematic?

(Q2) Could you give me figures for your loss ratios over the last few years?

Section F: Statistics

(Q1) If interview has proceeded well, ask for raw data:

Firm Size (GPI), reinsurance activities, expense ratios, loss ratios, underwriting profits, investment income, capital fund, from when company started operations to date.

(Q2) Request for copies of annual reports and accounts.

Section G: General

Additional relevant information

Check-list

(A)	Introduction	( )
(B)	Market Structure	( )
(C)	Market Behaviour	( )
	Product	( )
	Intermediaries	( )

	Investments	( )
(D)	Public Policy	( )
(E)	Claims	( )
(F)	Statistics	( )
(G)	General	( )

Appendix C: Interview Guide: The Insurance Department

Interview Guide: The Insurance Department

Section A: Insurance Department Structure

(Q1) What is the present structure of the Insurance department?

How has this changed over the time period under consideration?

(Define structure in terms of levels of hierarchy from the top to the bottom).

Personnel

Q1(a)) How many staff are there in the Insurance Department?

(b) What is the composition of the personnel, that is, Lawyers, Economists, Statisticians e.t.c.

(c) What is the position of these personnel in terms of the organisational hierarchy?

(d) Are all levels of staff involved in public policy making? How?

(e) What is the level of staff turnover? High? Low?

(f) Reasons for the above?

(g) Do Insurance Department staff leave to take up appointments in the insurance industry?

(h) Vice versa?, that is, do experienced people from industry come in to work at the agency?

Q(2) Who appoints the Director of Insurance? Other senior officials?

Q(3) Does the Director of insurance appoint his own staff?

Q(4) Who appoints the Managing Directors of NICON, Nigerian Re and African Re ?

Section B: Insurance Department Behaviour

Q(1) How does the Department make regulatory decisions?

(Q2) Who initiates the making of insurance laws? The agency? The industry? Others?

Q(3) To what extent does the industry participate in public policy making directly relevant to the industry?

(a) Formally?, that is, representation on the various committees.

(b) Informally? How?

Q(4) How are the potential costs/benefits of potential insurance laws to the industry assessed?

(b) How are the benefits to the consumer assessed?

Q(5) How is policing/compliance with the rules and regulations carried out?

Q(6) How is the effectiveness of the work of the agency measured?

Q(8) What are the difficulties encountered by the agency in the implementation of regulatory measures?

Q(9) In what particular areas of insurance supervision does the

agency experience difficulties with non-compliance with rules?

Q(10) How is this dealt with?

Q(11a) Does the insurance industry cooperate closely with the agency?

(b) If yes, in what ways?

Q(12a) How many insurance firms have had their licenses cancelled since 1976?

(b) Life firms, Brokers , Agents?

specific figures needed

Q(13a) How many insolvencies have occurred in the general and life market since 1976?

(b) What are the causes of these insolvencies?

Q(14) Are members of the regulatory agency allowed to have interests in the industry, for example, membership of boards of insurance companies, shareholdings?

Section C: General

(Generated from the discussions)

Check List

A Department Structure

B Personnel

C Department Behaviour

Regulatory decisions

Costs/benefits

Policing/compliance

Difficulties in supervision

Industry compliance

Revocation of licenses

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Table A13
Definitions of Variables Employed in Regression Analyses

VARIABLES	DEFINITIONS
Ownership	
**FOR	Foreign Life Offices
**NAT	National Life Offices
Structure	
**COMP	Composite Life Offices
Size	
LP	Life Premium Income
LogLP	Log of Life Premium Income
1/LogLP	Reciprocal Log Life Premium Income
1/P	Reciprocal Life Premium Income
SL	Size of Labour Force
A/SL	Total Assets per Size of Labour Force
*LP/SL	Labour Efficiency
LogA	Log of Assets
CR_{t-1}	Capital & Reserves in year t-1
**B1	Life Fund in excess of ₦20million
Financial	
NP/LP	New Life Business (% of Life Premiums)
GP_{t-1}	Goup Life Insurance in Force in year t-1
NB_{t-1}	New Businesss Underwritten in year t-1
LR_{t-1}	Lapse Ratio in year t-1
GS/TA	Poportion of Total Assets in Govt Stock
BS/TA	Poportion of Total Assets in Private stock
*ROA	Return on Invested Assets
*AC	Average Cost Ratio
*OE	Operating Costs Ratio
*ME	Management Expense Ratio
*Claims	Claims Ratio
*RR	Retention Ratio
Regulatory Periods	
**MIL	Military Administration
**OIB	Oil Economy
**$DEC59^{+4}$	Regulatory Lag Period

*Denotes independent variables
**Denotes dummy variables