

Finnish Insurance Today



FEDERATION OF FINNISH
INSURANCE COMPANIES

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Insurance market

A country of five million inhabitants, Finland is home to an insurance market which is small by international standards, covering less than two per cent of the EU insurance market. Even so, the Finnish insurance industry is an advanced market, and insurance plays a major role in society. The volume of premiums written accounts for nearly nine per cent of Finland's gross domestic product, and insurers' investments cover 59 per cent of GDP. Both figures are slightly above the EU averages. The high rates are explained by statutory employee pension insurance, which is included in the figures and accounts for a major share of the total.

There are 67 insurance companies operating in Finland, and 21 of the total are branches of foreign insurers (the figures date from January 2005). Besides insurance companies, the Finnish insurance market accommodates more than a hundred insurance associations, which are local mutual insurers engaging in non-life business. Statutory earnings-related retirement security is provided by not only insurance companies authorised to write employee pension insurance but also pension funds, both company-specific and industry-wide, which total 35 and 8, respectively. Insurance companies are divided according to their line of business into life, non-life, employee pension and reinsurance companies. One company may engage in one line only.

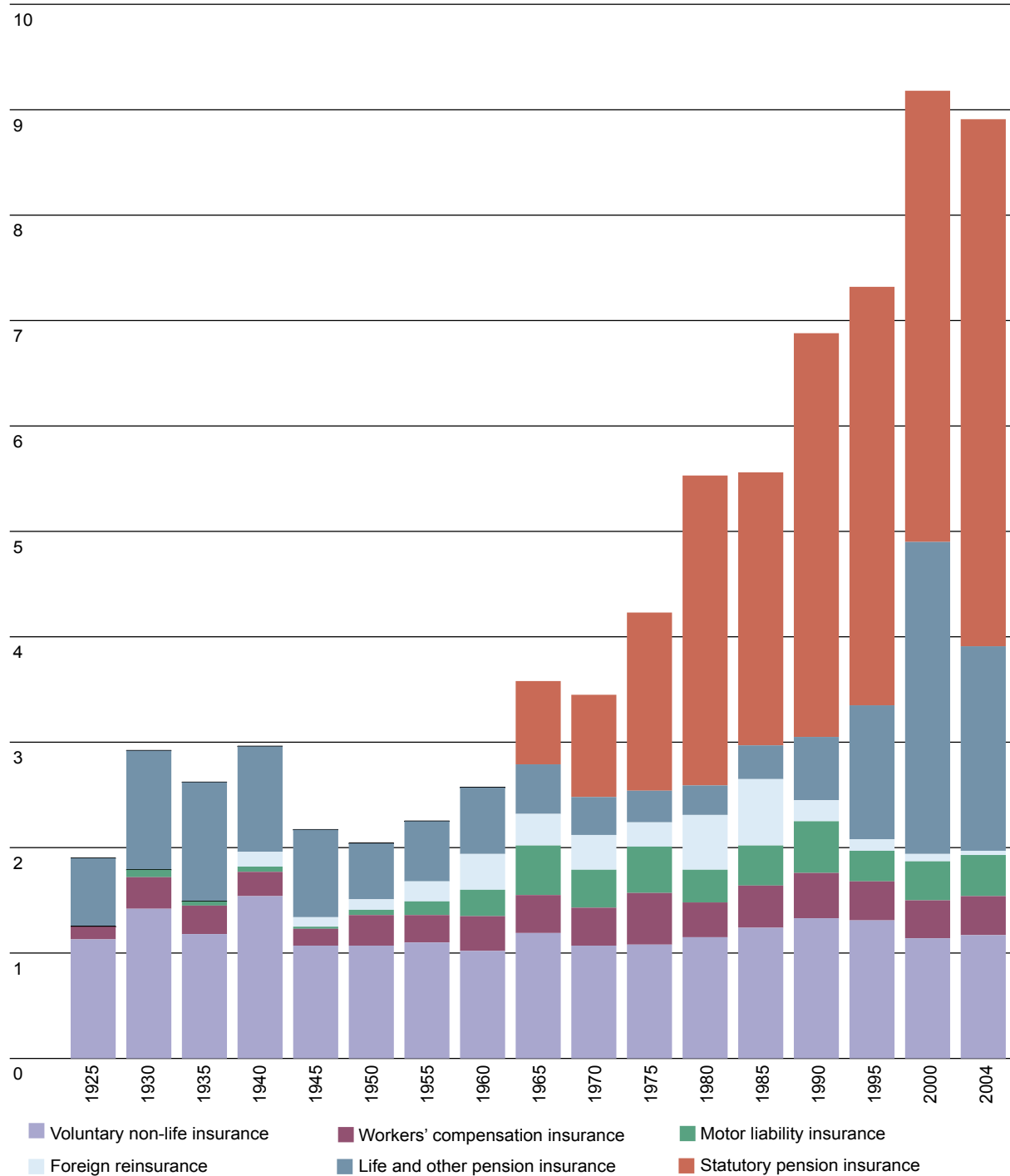
Insurance companies are either mutual or limited companies. The first limited companies entered the Finnish insurance market in the latter half of the 19th century. Today more than half of Finnish insurers are limited companies. One group of insurers may comprise both mutual and limited companies. Authorised pension companies, which are governed by restrictions on distribution of profits to the company's owners, are mostly mutual companies. By contrast, non-life business and personal life insurance are dominated by limited companies.

Under a long-established practice, Finnish insurers are seeking to provide their customers with a full palette of insurance services. As a result, most corporate customers buy their life, non-life and pension cover from insurers of the same group or alliance. Household policies also provide fairly extensive coverage today and are far more popular than policies taken out against single risks.

The Finnish insurance industry makes up a fairly concentrated market, where the four largest groups command some 80 to 90 per cent of the market for individual insurance lines. But the situation is much the same in the other Nordic countries and in any other country equal to Finland in size.

**Premiums written in different groups of insurance classes in 1925 to 2004
As a percentage of GDP**

Insurance classes were regrouped in 1995



Finnish insurers use a variety of distribution channels to make their services available to customers. While the bulk of corporate business is done through full-time sales personnel, company branches play a major role in household insurance. Most companies have a number of tied part-time agents who work exclusively for one insurer or one insurer group, though policies are also sold through several insurers' joint agencies, such as car dealers and travel agents. On the life insurance front, banks constitute a sizeable distribution channel. Insurance sales over electronic facilities such as the internet are on the increase. Brokers play a growing role, specialising chiefly in business insurance and life insurance.

The Finnish insurance market has been shaped by intense competition over the years.

In the early 1990s life insurance accounted for a mere ten per cent of insurers' gross premiums written but by the end of the decade the proportion had risen to one quarter. Life insurance assets accounted for 16.3 per cent of households' financial assets at the end of 2004, way up from 3.7 per cent in 1990.

Foreign insurance companies authorised to carry on business in Finland operate on a modest scale, covering a mere couple of per cent of the market. Life insurance is a stronger area for foreign insurers than non-life business. The largest Finnish insurers are present in international markets either as shareholders in local or international companies or through wholly owned subsidiaries. In recent years Finnish insurers have strengthened their footing around the Baltic Rim in particular.

The Finnish insurance scene

An integral part of social security

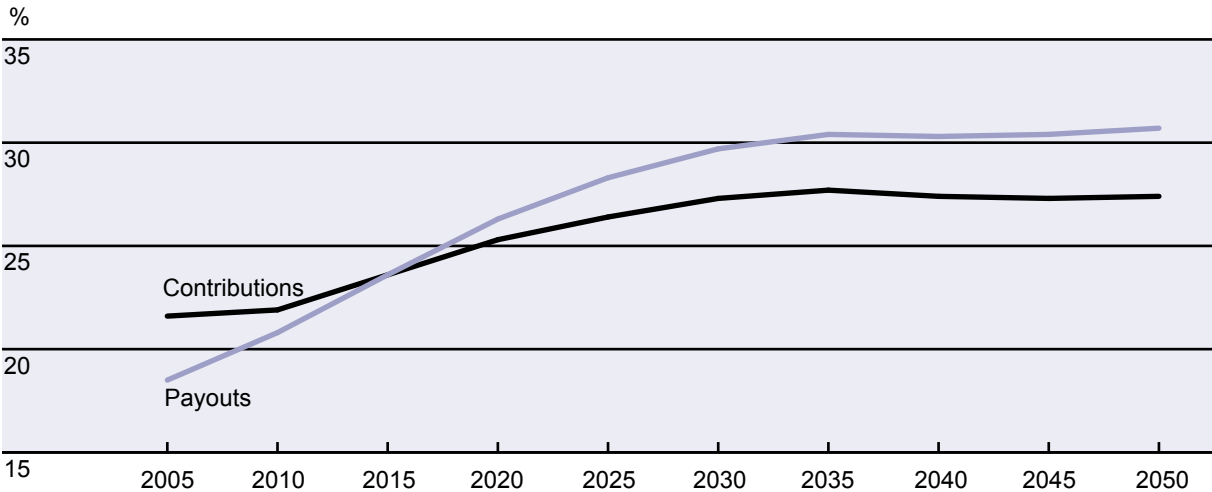
Finns have been building their social security under the concept known as the Nordic welfare state. The system ensures that all residents are entitled to public services and income protection, which is made up of minimum benefits and supplementary earnings-related benefits, both paid under compulsory schemes. Characteristic of the system is that public services, which include education, health and social services, absorb the lion's share of public funds spent on the welfare system, and the pattern ensures an even distribution of income.

The minimum benefits are funded with taxes and benefits are paid to people who are unable to earn an adequate living otherwise.

The benefits are largely means-tested and their level is not tied to earlier wages. Seen from an international perspective, Finnish minimum benefits are slightly higher than the average in western Europe.

The statutory earnings-related income protection schemes encompass nearly all employees, self-employed persons and farmers residing in Finland. Statutory motor liability insurance and workers' compensation insurance provide full compensation for loss of income. Statutory health insurance and employee pension insurance benefits depend on the period of employment and level of earnings, amounting to a maximum of 70 per cent of earnings in health insur-

Pension payouts and contributions, %



Private-sector pension payouts and contributions as a percentage of payroll.

ance and up to 60 per cent in employee pension insurance, calculated on the average earnings of the person's working life. This level may not be reached because of eg gaps in career paths, but the level may also be exceeded particularly if the person continues to work beyond 63. Statutory earnings-related benefits accrue on all earnings without any upper limit.

The minimum benefits scheme and the statutory health insurance scheme are managed by the state run Social Insurance Institution. Statutory motor liability and workers' compensation insurance, instead, is provided by privately owned non-life insurance companies. Authorised employee pension companies, which are privately operated businesses, provide compulsory pension insurance to nearly all private-sector workers in Finland. Social partners have also agreed on a group life insurance arrangement which covers all employees. This insurance is available from private life insurance companies.

Thanks to the wide coverage of statutory earnings-related benefits, and partly also the adequate level of benefits, the need for utilising life or personal pension insurance was less acute in Finland than in many other western industrialised countries up to the first half of the 1990s. But the situation changed when cuts were prompted in statutory benefits not only by the recession but also by the prospect of ageing population, which made it necessary to start preparing for additional expenses. As a result of this development, put together with increased

wealth overall, gaps in careers and international mobility, households now feel they have more reason to supplement their statutory benefits with eg life, voluntary pension, personal accident and health insurance policies.

Public social and health services are provided in Finland by municipalities and financed with both taxes and fees charged to customers, though the fees do not cover the cost of providing the services. People who are injured in job-related accidents and road accidents are treated under the public health care scheme, and the actual cost of this care is covered by workers' compensation and motor liability insurance, both statutory lines. Public welfare services, which were built in Finland in the 1970s and 1980s, used to be so extensive and of such a high standard that there was little need for private services. In the early 1990s, however, public services started to show some lack of both quality and availability, weakened by financial straits in the public sector. This development boosted the use of private services and accentuated the need for funding the cost of public sector services with insurance-based solutions.

A major share of Finnish insurance cover and social welfare is provided by statutory insurance schemes. Such compulsory lines of insurance, regulated by separate pieces of legislation, include employee pension, workers' compensation, motor liability, patient and environmental insurance.

Employee pension insurance

Private-sector employees' pension cover is provided by privately owned insurance companies and pension funds, either company pension funds or industry-wide schemes. Public-sector employees, instead, are insured under specific institutions such as the Local Government Pensions Institution and the State Treasury. Although managed by separate bodies, the pensions are determined according to more or less equal principles. Social partners are represented on the administrative bodies of employee pension institutions.

Finnish employee pension insurance is not covered by EU insurance directives. Although it is earnings-related, employee pension insurance is a statutory cover available to all employees and therefore comes under the first pillar in the EU classification. The principles of insurance directives cannot be applied to Finnish employee pension insurance because the pension benefits accrue by the same rules no matter where the employee is insured and because the proportion of benefits funded on a pay-as-you-go basis is substantial. In this setting, the institutions authorised to participate in the system share the expenses of the payouts, which naturally has to be done according to uniform rules. Such rules would not fit the home country principle of financial supervision.

Foreign insurance companies are free to set up or buy authorised employee pension insurance companies in Finland. Their operations are governed by the same conditions as Finnish companies' operations, once the

company has been granted a licence to carry on business by the Ministry of Social Affairs and Health.

Private-sector employers are required to cover their employees under employee pension insurance in accordance with the Employees Pensions Act. Companies with more than 300 employees may set up a company pension fund or an industry-wide pension fund for the purpose.

The Finnish employee pension scheme is a partly funded, defined-benefit scheme. Current payouts absorb about three quarters of pension insurers' premiums and investment income, and the remaining one quarter is funded to cover future pension benefits.

Besides retirement benefits, employee pension insurance protects against disability, breadwinner's death and, in some cases, against longterm unemployment. Rehabilitation is one of the benefits included in the pension scheme. Rehabilitation may be given, where deemed appropriate, to prevent disability or to improve work capacity.

At the start of 2005, the Finnish employee pension scheme underwent a reform. Pension benefits are now calculated on income earned annually over the whole working life, not separately for each period of employment. Pension benefits accrue at 1.5 per cent of annual earnings up to age 53, after which the rate rises to 1.9 per cent. At 63, the accrual rate rises to 4.5 per cent. The age at which employees start to earn pension and employers become liable to insure falls from 23 to 18 years.

There is no upper limit to income earned by pensioners under the employee pension scheme. If a retiree's employee pension is large enough, the person is not entitled to national pension at all. The benefits ensured by the employee pension scheme may naturally be supplemented by voluntary pension provision, both personal and collective.

Under the present pension system, employees may retire on old-age pension at age 63 but if they choose to work later they earn pension until age 68. The average retirement age is about 59 years, because very often people retire on disability or unemployment pension before reaching the actual retirement age. The latest reform was designed with an aim to raise the retirement age gradually by three years eg by removing unemployment pensions, by introducing

economic incentives and, above all, by restructuring working life. This is the biggest challenge for Finnish pension policymakers today.

Self-employed persons and farmers are covered by their own statutory pension schemes, which largely follow the principles of the employee pension system. These schemes are partly funded by the state.

Employee pension benefits are funded with wage-based contributions made by both employers and employees, which have to be approved by the government every year. In 2005, employers contribute an average of 16.8 per cent of the payroll and employees younger than 53 contribute 4.6 per cent, while 53-year-olds and older employees contribute 5.8 per cent of their monthly pay.

**Fresh funding collected for payouts
under different pension schemes in 1994 to 2003, € million**

	National pensions	Compulsory pensions (employee, motor liability, workers comp)	Voluntary pension plans
1994	3,123	8,027	420
1995	3,147	8,470	635
1996	3,081	8,899	546
1997	3,009	9,271	723
1998	2,891	9,698	854
1999	2,791	10,201	1,059
2000	2,707	10,715	1,662
2001	2,740	11,522	1,767
2002	2,792	12,327	1,852
2003	2,766	13,100	1,938

Employee pension insurers compete with each other by allowing premium discounts to customers from the company's profits. Owners who have injected capital into authorised employee pension companies are allowed to be paid a reasonable return slightly above the rate of risk-free rate of interest.

The reformed system takes account of the increasing life span: pension accrual is regulated by a factor which reflects the person's life expectancy. In this setting, increasing life span poses no risk to the Finnish employee pension scheme. Moreover, the system will simplify when the new pension act for all private-sector employees takes effect in 2007, replacing three separate pieces of pension legislation now governing employees, temporary employees, and freelance employees.

Voluntary life insurance

Finnish life insurance, which includes voluntary life and pension insurance, accounts for nearly one quarter of all premiums written by Finnish insurers. Life insurers' 2004 premium volume amounted to €2.9 billion. Roughly 80 per cent of the total came from policies taken out by personal customers, while the rest came from corporate customers.

More than half of the premium volume, or 56 per cent, originated from savings policies in 2004. Individual pension plans accounted for 27 per cent of the total and group pension policies for 7 per cent. Another 7 per cent was covered by pure-risk life policies. A growing product within this line was loan insurance, which has gained popularity in Finland: roughly one third of all loans are secured by loan insurance.

The figures for new life business reveal that the best performing products were savings policies and personal pension plans. Life savings policies accounted for 80 per cent of new premiums written and 55 per cent of the number of new policies sold. Personal pension plans covered 10 per cent

of new premiums written and 43 per cent of new contracts concluded. The policy term of personal pension plans is long: contributions are made over a period of 23 years on average.

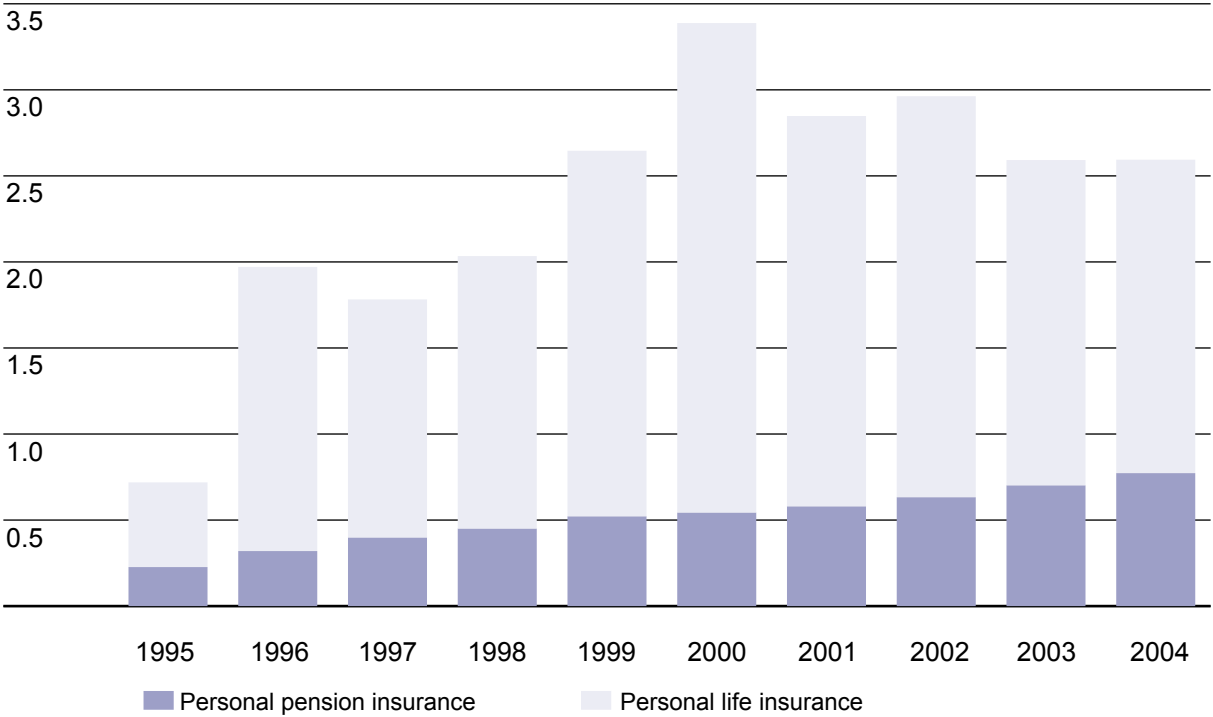
As much as 88 per cent of new premiums written comes from personal customers. New business written for commercial customers is largely made up of group pension policies. This line amounts to modest figures at the moment but employers' interest in providing employees with supplementary pension benefits is on the increase.

Life insurance products are either unit-linked or traditional life policies. Unit-linked

policies have gained popularity in recent years, accounting now for more than half of all new business written. Traditional life policies pay out interest at a guaranteed rate and a bonus from the insurer's profits.

The maximum rate of guaranteed interest paid on traditional life policies is 4.5 per cent on contracts concluded before 1999 and 3.5 per cent on policies issued from 1999 to 2002. In March 2003, the rate of guaranteed interest was lowered to 2.5 per cent, following the generally low level interest rates. These rate changes are based on a Ministry of Social Affairs and Health regulation.

Life and pension premiums written in Finland in 1995 to 2004, € billion
Weighted to reflect increases in cost of living index, 2004 = 100



Voluntary non-life insurance

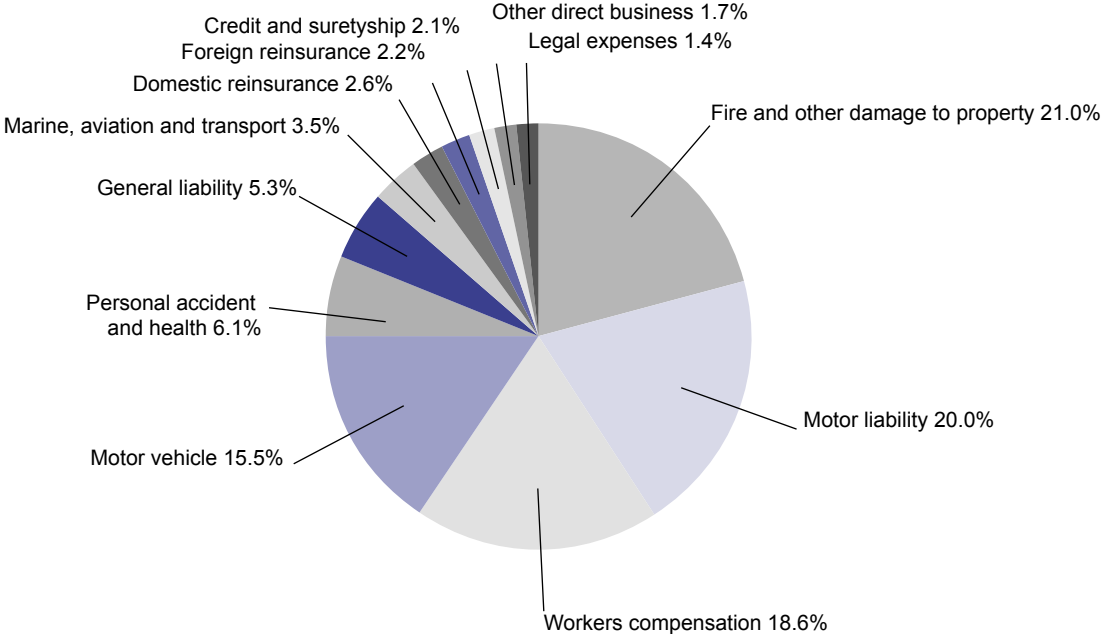
Voluntary non-life insurance accounted for nearly 11 per cent of the Finnish insurance market in 2004, amounting to about €14 billion. The largest lines of voluntary non-life business, in terms of premiums written, are insurance against fire and other property damage, car insurance and personal accident and health insurance. Although Finns have otherwise covered their property against risks fairly extensively, the country's vast forests are inadequately insured. The problem has gained attention now that storms are causing more and more damage in Finland too. Many property policies automatically include liability cover, eg household insurance and other package policies built around fire insurance. More than half of voluntary

non-life business is made up of personal policies and the rest is covered by commercial and institutional contracts.

Finnish insurers pay over 7,000 fire claims every year.

Measured in terms of premiums written, non-life insurance represents about two per cent of Finland's GDP, which is slightly below the European average. The low percentage is explained by a number of structural factors. For instance, the volume of voluntary health insurance is low in Finland and so is the level of risk in many lines of non-life business, thanks to extensive loss prevention work. Part of the low penetration of voluntary non-life insurance can be attributed to insurers' efficiency and harsh competition, which lowers premium rates.

Breakdown of non-life premiums written in 2004, total €2.9bn



Why health insurance is not significant for Finnish insurers is largely explained by the country's extensive public health care services, which are available to all people throughout the country. Statutory health insurance, managed by the Social Insurance Institution, provides extensive cover for loss of income, medical expenses and also private health care expenses resulting from illnesses shorter than one year.

Finnish non-life insurance policies are usually renewed automatically every year and do not expire unless specifically cancelled by either party. This is why holders of non-life policies stay with the same insurer more often in Finland than in many other countries.

In recent years, Finnish non-life insurers have improved their profitability a great deal. When non-life insurers' profitability is compared in the light of combined ratios, it is worth noting that Finnish companies' technical provisions amount to a higher figure than the European average. This is largely explained by pensions and other benefits paid under workers' compensation and motor liability insurance, both statutory non-life lines in Finland, because the duration of technical provisions needed for longterm payouts is long. In this setting, technical provisions can be covered with assets placed in longterm targets, and the income received on the assets makes it possible to reach the profitability level of companies with less technical provisions even if the combined ratio is high.

Statutory non-life insurance

There are four major lines of statutory non-life insurance in Finland: workers' compensation, motor liability, patient and environmental impairment insurance. Workers' compensation and motor liability insurance cover one third of all premiums written in non-life insurance.

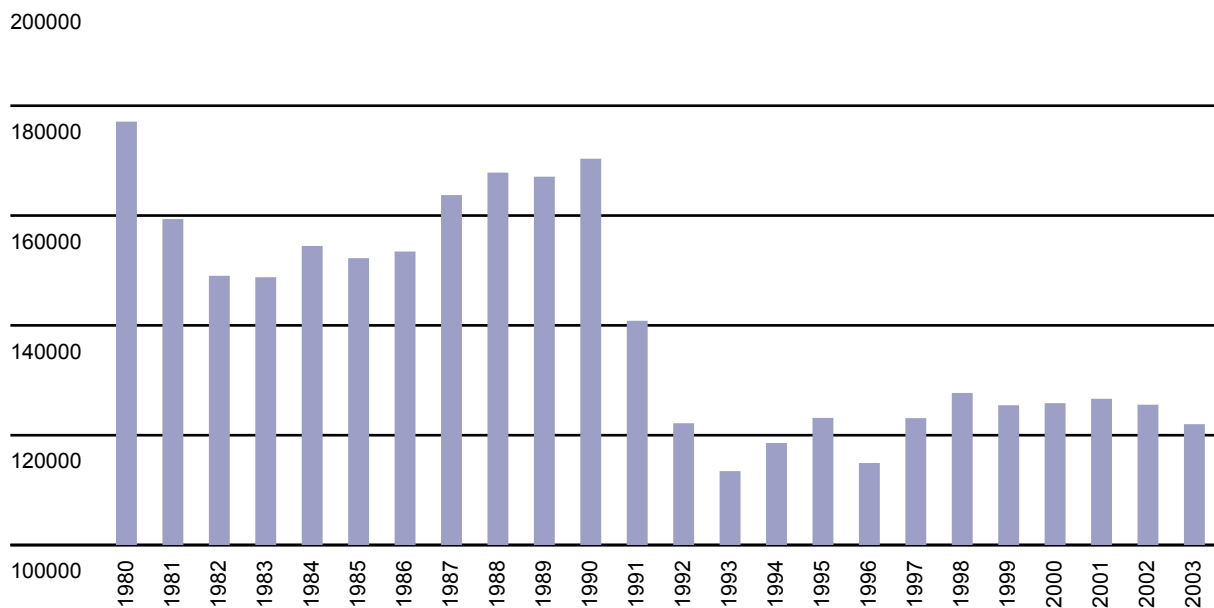
Workers' compensation insurance

On-the-job injuries and occupational diseases are covered by workers' compensation insurance law in Finland. Employers are required to insure their employees against workplace accidents with a non-life insurer. Compensation is paid regardless of negligence on the part of the employer.

The rate of workers' compensation insurance premium is calculated on the employer's payroll, varying according to the employee's occupation and the risks involved in the work. Large employers' premium rates are directly affected by claims experience. The average premium rate is 1.1 per cent of the total pay.

Workers' compensation insurance covers not only actual workplace accidents but also commuting accidents and occupational diseases. Compensable occupational diseases include gradually occurring diseases such as cancer resulting from longterm exposure to asbestos to the job. In recent years, Finnish insurers have been paying about one hundred asbestosis death claims a year, which is more than half of all death claims paid under workers' compensation insurance annually. The number is expected to stay

Occupational accidents in 1980 to 2003



The number of occupational accidents reported to insurers annually has come down from 170,000 in the late 1980s to 120,000 in the early 2000s.

high for several years ahead until the ban on asbestos use, popular in Finnish industry and construction in the 1970s, starts to pull the disease and death statistics lower.

Workers' compensation insurance covers medical expenses, daily benefits for temporary disability, disability pension, disability benefits and family benefits according to the principle of full compensation. All income protection benefits are taxed like earnings and given priority if coordinated with other social security benefits. In other words, the public scheme only pays compensation or benefits in respect of amounts in excess of the benefits due under workers' compensation insurance.

Motor liability insurance

Compulsory motor liability insurance covers all bodily injuries and property damage caused to third parties by use of motor vehicle in traffic. The insurance also covers injuries sustained by the driver himself, irrespective of fault, in most cases.

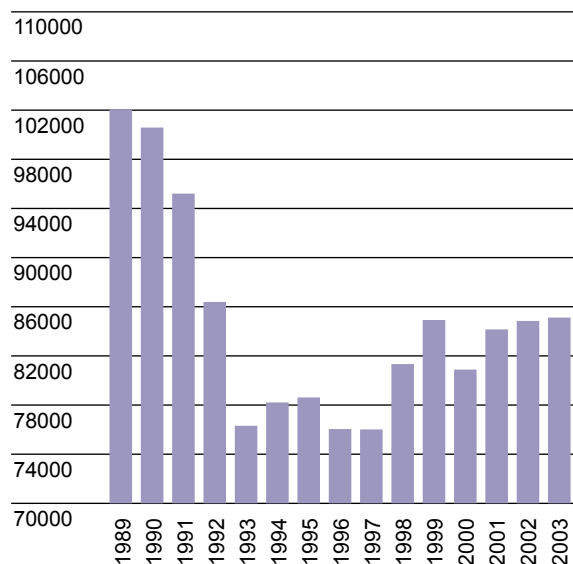
Practically the only cases where bodily injuries are not covered are injuries sustained by drunken drivers and persons who have failed to insure. Furthermore, compensation paid to third parties as a result of accidents caused by drink driving or another similar offence may be recovered from the liable party.

Motor liability insurance also covers material damage caused to the innocent party's vehicle and to any other property not owned by the liable party. Compensation for damage to the liable party's own vehicle, instead, is never paid under motor liability insurance. Protection against such damage can be obtained under voluntary car insurance, which many motorists take out.

Compensation for bodily injuries and property damage is paid in full to meet the actual costs incurred and losses sustained. There is no upper limit to the amount of compensation for bodily injuries. Like in workers' compensation, income protection benefits are given priority if coordinated with other social security benefits.

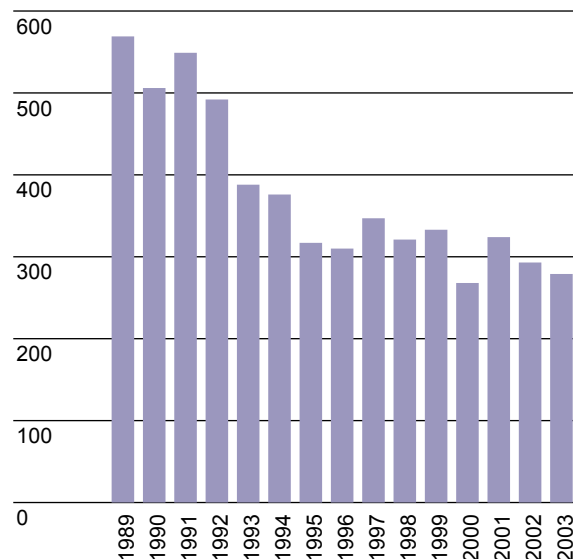
Compensation for bodily injuries covers medical expenses, pain and suffering, loss of income, home care, disability pension, permanent defect and handicap, rehabilitation, burial expenses and family pension benefits. Property damage to the innocent party's vehicle and to other property not owned by the liable party is compensated in full.

**Motor claims paid in 1989 to 2003,
all accidents**



Total number of motor liability claims paid by insurers.

**Motor claims paid in 1989 to 2003,
fatalities**



The number of road accidents rose in line with increased traffic volumes up until the late 1980s in Finland but in the 1990s the trend reversed. As the volume of road traffic increased at the same time, the fall in accident numbers is even more significant.

Patient insurance

Statutory patient insurance covers bodily injuries sustained by patients in connection with medical treatment or health care given in Finland.

Compensation for bodily injuries is paid for bodily injuries which are likely to result from an examination of a patient or other similar action taken or neglected.

Patient insurance does not cover consequences of any medically justifiable measures that could not have been avoided by use of other, equally effective methods of treatment. As a result, patient insurance does not cover consequences resulting from risks which are generally involved in medical examinations and treatment. Neither does patient insurance cover cases where appropriate treatment has not produced the desired outcome or where the patient has sustained slight injuries.

Compensation for patient injuries is paid by the Patient Insurance Centre. The amount of compensation is assessed in compliance with the provisions of the Damages Act and the standards applied by the Patient Injuries Board.

All persons engaging in medical treatment or health care operations under a right based on legislation must be covered by a patient insurance policy issued by an insurance company or by the Patient Insurance Centre.

Environmental impairment insurance

Compulsory environmental impairment insurance protects against damage and injuries sustained in cases where it is not possible to recover compensation in full from the business that caused the damage or injury and no compensation can be collected under the liable party's liability insurance, if any. Environmental impairment insurance also covers events where the primarily liable party has not been identified.

The primary liability for environmental damage falls on the party whose operations have caused the injury or damage. The liable party must compensate the environmental damage or injury in full, including the cost of prevention of environmental damage and the cost of remediation of the polluted environment.

Any private corporation whose operations involve a material risk of environmental damage or whose operations cause harm to the environment in general is required to take out an environmental insurance.

Environmental impairment insurance is available from all general liability insurers who are members of the Environmental Insurance Centre. Claims are handled by the Environmental Insurance Centre.

Loss prevention

Loss prevention makes up a crucial part of insurance business in Finland. Shouldering their share of social responsibility, insurers make use of the experience gained from occurred accidents for the benefit of loss prevention. Insurers' efforts to reduce claims costs through loss prevention translate into benefits reaped by customers in the form of lower insurance premiums.

The insurance industry focuses on fields of life where accidents are frequent but can be prevented from happening with reasonable measures.

Insurers' loss prevention work also covers inspection and approval of safety equipment, approval of companies installing the equipment, and safety advisory services. Moreover, insurers encourage loss prevention in policy terms eg by allowing discounts for use of equipment and companies approved by insurance companies. The approval and inspection systems are operated parallel to and in close cooperation with the relevant authorities. Insurers' loss prevention efforts gain a pronounced position in areas which are not regulated by authorities, such as structural burglar protection.

Prevention of occupational injuries, road accidents and accidents in the home and leisure time activities is supported by regulations, campaigns and special organisations, with the involvement of both authorities and insurers. Workplace accident prevention is funded with a two per cent charge loaded into workers' compensation premiums and used for occupational safety research and distribution of workplace safety information. Road safety work, instead, is funded with a 1.2 per cent charge included in motor liability insurance premiums, and the work focuses on research and education promoting road safety in Finland. Fire insurance risk premiums include a three per cent charge which is used for promotion of fire safety, notably fire brigade investments and fire prevention work.

Insurers' long-range work has paid off. The number of injuries and deaths sustained in motor traffic has fallen dramatically over the decades, although the volume of traffic has increased many times over at the same time. Workplace accidents, both injuries and deaths, have also been reduced substantially by effective accident prevention. As to home

and leisure-time accidents, instead, the trend is worrying; home accidents injure and kill more people today than earlier. Part of this increase results from ageing population and increased use of alcohol.

Finnish insurers' contribution for the prevention of fire losses consists of inspections, precautionary measures and safety training given to persons engaging in hot-work operations, who are required to have an in-force hot work card issued on successful completion of a safety training course. This training has significantly reduced the number of fire losses caused by hot-work operations. In cooperation with other interested parties, insurers run information campaigns promoting prevention of losses caused by fire and burst pipes. Over the long term, fire losses have come down in Finland and burst pipes damage has increased.

Finnish insurers also draft precautionary guidelines encouraging customers to duty of care over their property. As part of policy conditions, precautionary guidelines are binding on the policyholder. Non-life insurers work together with authorities to improve fire investigation methods and tackle electric fires. Insurers are also actively involved in the implementation of a nationwide internal safety programme launched by the government.

Crime prevention and investigation is a field where insurers work in cooperation with security authorities. The focus areas are property protection and prevention of burglary, fraud, drug-related crime and arson. Extensive work in insurance fraud investigation has resulted in new prevention tools devised in cooperation with other European

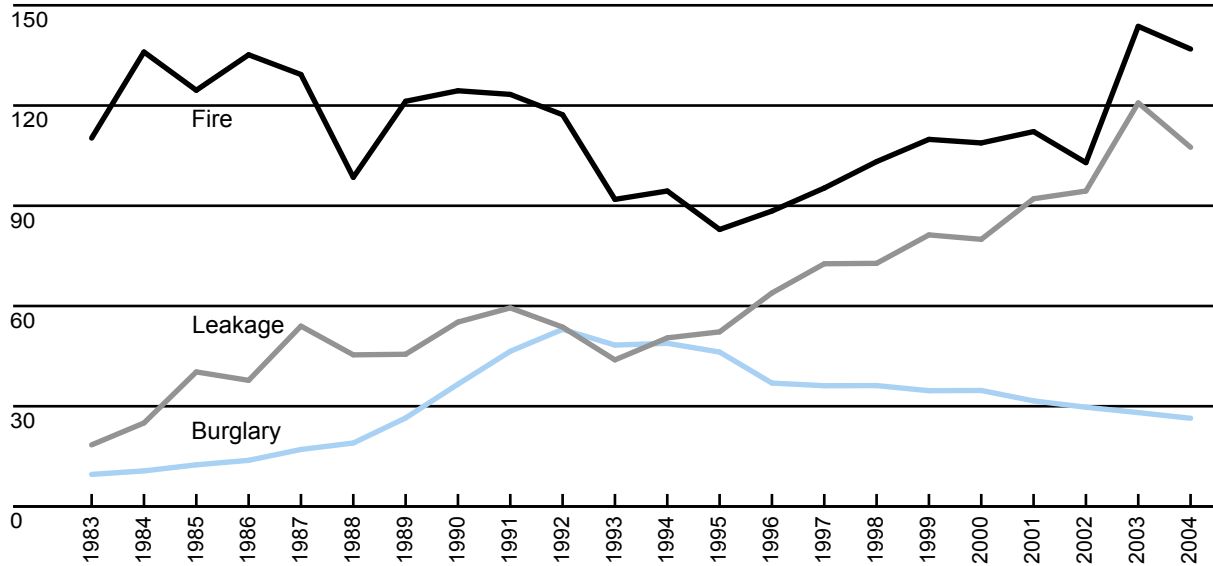
insurers. Prevention of life and pension insurance fraud operates through a network built between insurers and security authorities. Most insurance companies have their own insurance investigators who specialise in crime investigation.

Finnish insurers have a joint claims register set up with an aim to prevent customers from getting compensation from several insurers for the same loss. Over time, the claims register will also reveal persons that sustain losses of a certain kind exceptionally often. As customers are told about the existence of a claims register when they file a claim, or even earlier, the role of the claims register as a fraud deterrent is significant. No data recorded in the database may be used for customer selection or for marketing.

Moreover, Finnish insurance companies have a joint register for fraudulent claims. The fraudulent claims database contains details of customers who have committed insurance fraud.

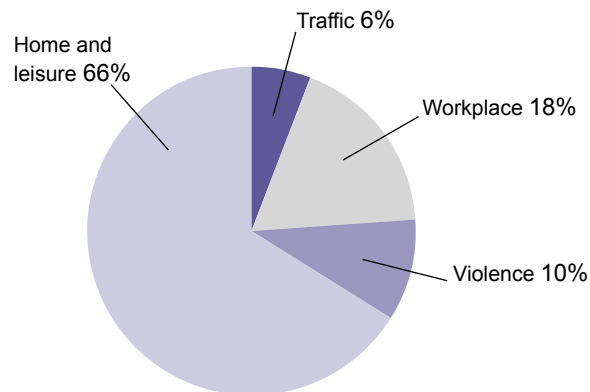
Loss prevention and safety work continue to face major challenges in Finland. Although accident probability has decreased significantly in traffic and workplace accidents, home and leisure-time accidents are frequent. It was only recently that the government allocated new resources for the prevention of accidents in the home and in leisure-time activities. The risk of these accidents increases with ageing population. Finnish authorities, insurers and many voluntary organisations are working to devise ways of preventing accidents by means of cooperation and campaigns.

Fire, burglary and leakage claims paid in 1983 to 2004



Fire claims cost Finnish insurers €137m in 2004. Claims paid for leakage damage have grown nearly six-fold in twenty years from €17m to €100m. The growth of burglary claims has reversed and claims are now paid for about €30m a year.

Accidents and violence



The number of accidents occurred in Finland annually stands at about one million, out of which 700,000 happen in the home. Source: National Public Health Institute

Investment

Finnish insurance companies manage asset portfolios which are comparatively large compared to premium income, calculated at current values. Much of this is explained by the country's partly funded employee pension scheme, which is operated by authorised employee pension insurers. Another feature that affects the situation is the practice where benefits due under workers' compensation and motor liability insurance are paid in annuities instead of lump sums, in compliance with the relevant laws. This creates longterm provisions for annuity payouts in insurers' balance sheets, which in turn makes it possible to invest the assets in longterm targets. Thirdly, insurers' investments have been boosted by the emerging popularity of voluntary pension and life insurance savings policies. Although non-life insurers' solvency margins have narrowed in recent years, they are still at a healthy level. By contrast, life and employee pension insurers have reinforced their solvency substantially in recent times.

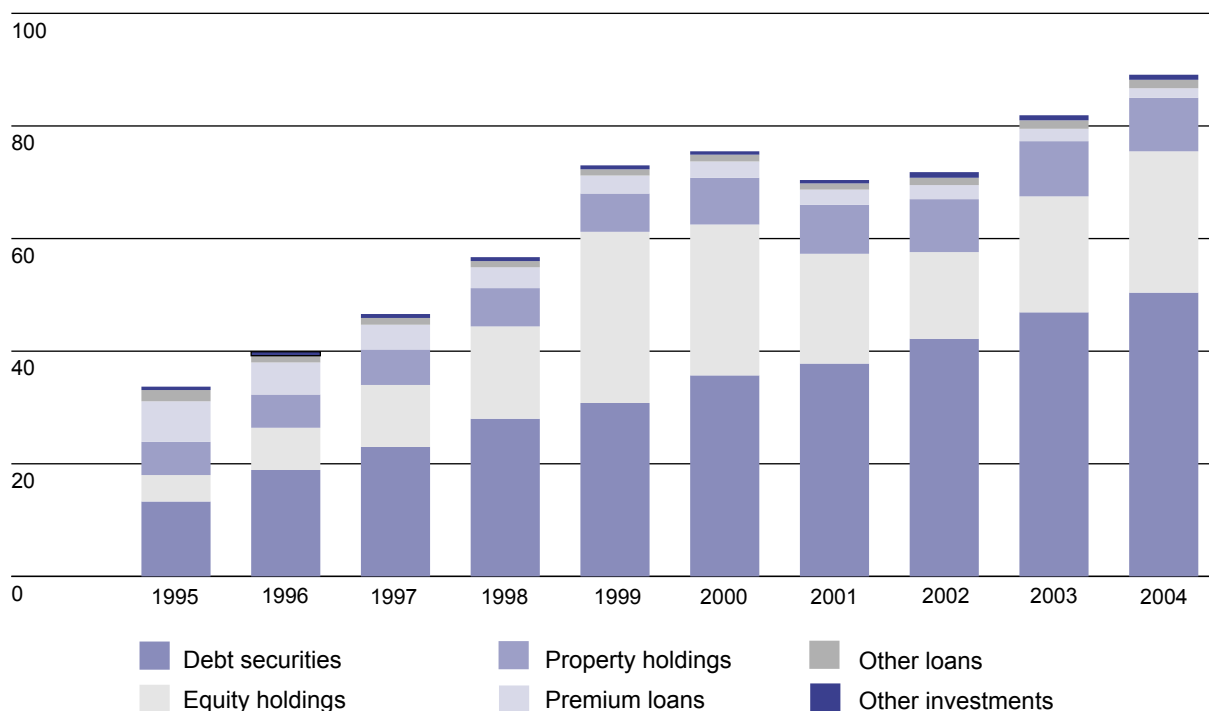
Calculated at current values, Finnish insurers' investment portfolio amounted to €89 billion at the end of 2004, an amount which is six times the volume collected in gross premiums annually and equals 59 per cent of Finland's GDP. The bulk of these assets, worth €55 billion, were owned by Finland's unique authorised pension insurers. Life insurers' investments totalled €25 billion and the remaining €9 billion was covered by non-life insurers.

Finnish insurers' investment policies have seen a radical change over the years, in the wake of deregulation in the Finnish financial market in the late 1980s and early '90s. In the 1980s, three quarters of insurers' investment business was tied to customers: insurers lent money to their corporate customers, and the customers often worked in premises rented from the insurers. Since then, customer-linked investment has fallen below one tenth of the total. Another major change on the investment scene is that insurers have been vigorously diversifying their investments out of Finland, which used to be the focus of their investment.

Finnish insurers have been placing their funds in capital markets, not least in debt securities and equities. Half of insurers' assets consist of debt securities, mainly bonds, and equities cover one quarter of the portfolio. Given that Finnish insurance companies are very solvent, seeking higher investment returns than earlier, the weight of equities is likely to grow in the future. Properties account for 9 per cent of the total investments.

At the end of 2004, 40.5 per cent of Finnish insurers' investments were in Finland, 42.6 per cent in the euro zone and 16.8 per cent in other countries. Foreign assets largely consisted of bonds, equities and fund investments. Finnish insurers continue to diversify their assets out of the country's small capital market.

Finnish insurers' investments at current value in 1995 to 2004, € billion



Insurance and taxation

Taxation of policyholder

Taxation of life insurance

Premiums paid on life and health insurance policies are not deductible in taxation.

Benefits paid under life insurance savings policies are taxable capital income to the beneficiary, taxed at 28 per cent. If the amount is paid to the insured policyholder or the policyholder's close relative, tax is levied on the return earned on the policy. The return is calculated by deducting the total of premiums paid on the policy from the savings accrued. If the benefits are paid to the policyholder's close relative free of consideration, the capital, ie the premiums accrued under the policy, is subject to gift tax in respect of amounts exceeding the equivalent of €8,500. Premiums paid over the past three years qualify as tax-exempt up to this limit. If the savings accrued are paid to a beneficiary other than the above-mentioned, the whole amount is treated as taxable capital income.

Lump-sum death benefits paid under pure life insurance constitute either tax-exempt income to the beneficiary in income taxation, with part or none of the amount subject to inheritance tax, or taxable capital income in respect of the whole amount. Taxation is determined according to the family connection between the insured and the beneficiary. Close relatives receive the benefits tax free up to about €35,000. Amounts in excess of this limit are subject to inheritance tax. If the beneficiary is the surviving spouse, half of the amount received, a minimum of €35,000 in any event, is exempted from inheritance tax. If the death benefit is paid to a beneficiary other than a close relative,

all of the amount is treated as taxable capital income.

Health insurance and personal accident benefits are tax exempt if paid to compensate for expenses incurred. Loss of income benefits, instead, represent taxable earnings, unless paid under hospitalisation insurance for hospital treatment, in which case tax is only paid on amounts exceeding the treatment fee. Lump-sum benefits received on account of permanent disability or severe illness are tax-free income.

Contributions to personal pension plans may be deducted in taxation, and no tax is levied on the return earned during the period when premiums are paid in. Future pension payouts, instead, are taxable income to the recipient. Pension contributions are deductible in capital gains taxation up to €5,000 a year. If the taxpayer has no capital gains, the pension contributions are deducted in income taxation. This tax relief is granted on the condition that pension payouts start at 62 years at the earliest. Payouts under personal pension plans are taxed at the capital gains tax rate.

Contributions made by employers for statutory employee pension insurance policies are deductible operating expenses in Finland. These contributions are in no way treated as taxable income to employees. Employees, instead, may deduct their own employee pension contribution in taxation. Employee pension payouts are also taxed as earnings, according to a progressive tax scale.

When paying out pension benefits to retirees, insurers withhold the tax in advance.

Taxation of insurer

Taxation of insurance companies

Finnish companies, including insurers, are taxed on the basis of profits shown in their annual accounts at a flat rate of 26 per cent.

Dividends received by insurers on investment assets are free from tax up to 25 per cent and the 75 per cent is taxable income. This leads to a situation where dividends on investment assets channelled through insurance companies and other financial service companies are taxed several times. This is against the general principle of avoiding multiple taxation.

There are other special aspects to insurer taxation such as taxability of increases in the value of investment assets recognised in financial statements.

Indirect taxation

In line with the practice applied in the other EU states, Finnish insurers are not liable to pay VAT on any insurance services sold or mediated by them. Finnish VAT law provides an exhaustive list of insurance services exempted from taxation, and the law is interpreted strictly in both fiscal and legal practice.

The rate of VAT generally applied to sales of goods and services is 22 per cent.

Insurance premium tax

Premium tax is imposed on non-life premiums on voluntary insurance contracts covering risks located in Finland. Premium tax is paid to the state by the insurer, if the insurer engages in business in Finland. If the insurer does not carry on business in Finland, the policyholder must pay the tax.

No tax is charged on premiums payable on contracts constituting insurance of the person, credit insurance, reinsurance, cargo insurance or on contracts covering goods exported from, imported to or transported through Finland or on contracts covering transport equipment.

The tax rate is 22 per cent of the premium, net of tax.

Besides premium taxes, insurance companies are required to collect a number of other charges for the state, such as road safety charge and fire brigade charge.

Insurance legislation

The operations of insurance undertakings are regulated by the following core pieces of legislation:

- Insurance Companies Act which governs Finnish insurance companies;
- Employee Pension Insurance Companies Act which governs companies carrying on statutory employee pension insurance business;
- Insurance Associations Act which governs local mutual non-life insurance associations;
- Foreign Insurance Companies Act applicable to foreign insurance companies registered in either EEA countries or third countries;
- Insurance Mediation Act governing the operations of insurance brokers and agents; and
- Insurance Contracts Act which governs insurance contracts.

Legislation governing certain lines of statutory insurance is described under section The Finnish Insurance Scene.

Insurance Contracts Act

The Insurance Contracts Act sets forth provisions on the rights and obligations of not only insurers and policyholders but also the insured, beneficiaries and certain third parties. The core aim of the law is to protect insurance consumers, which is reflected eg by the fact that the provisions are mandatory for insurers in favour of consumers. This means that insurers may not deviate from the provisions of the law in their policy terms to the detriment of consumers. The same protection is provided for self-employed persons and small businesses which in respect of their knowledge, skills and financial resources can be compared to consumers.

National insurance contract laws have not been harmonised within the European Union. Instead, the EU has issued regulations on the laws to be applied to cases where the insurer and policyholder are from different member states. Provisions on these choice of law questions are set forth in the Finnish Act on legislation applicable to certain insurance contracts of international nature. According to this law, a foreign insurer who does not have a branch in Finland and who markets its insurance products in Finland may provide in its policy terms that the law applicable to the contract is the law of his home state only if the home state law ensures that consumers' rights are at least equal to those ensured under the Finnish Insurance Contracts Act.

The following highlights the content of the Insurance Contracts Act:

- The conclusion of an insurance contract always requires exchange of information between the parties. As a result, the law imposes the duty of disclosure on the contracting parties, and the duty of disclosure on the insurer is strict. Before concluding an insurance contract, the insurer is required to give the customer all information needed by the customer to assess his insurance need and to choose the cover, such as details of the insurer's insurance products, insurance premiums and insurance terms. All major exclusions must also be pointed out to the customer. The duty of disclosure is not fulfilled by a mere delivery of policy terms. If an insurer or its representative has failed to give the necessary information on the insurance concerned or has given incorrect or misleading information, the insurance contract is considered to be in force to the effect understood by the policyholder on the basis of the information received. During an insurance period the insurer is required to inform the policyholder annually of the sum insured and of any other relevant circumstances relating to the insurance, such as deductibles and, in the case of life insurance policies, surrender value.

- Though the length of an insurance period may be agreed case by case, most non-life policies are annual contracts. Life insurance policies are often continuous contracts valid until further notice. The policyholder may at any time terminate an insurance contract during an insurance period. The insurer's right to terminate a contract is restricted.
- The policyholder is usually required to pay the insurance premium within one month from the date that the insurer sent the invoice. If the policyholder fails to pay the premium, the insurer may terminate the contract at 14 days' notice. Only in exceptional cases can payment of the premium be set as a condition for the commencement of a contract.
- The insurer is required to decide on a claim within one month from the date of receipt of the documents and information needed for the decision. If an insurer fails to pay an accepted claim within this period of time, the insurer is required to pay penalty interest on the delayed payment of compensation or benefit.

An English translation of the Insurance Contracts Act is available on the website of the Federation of Finnish Insurance Companies at www.vakes.fi/svk.

Other consumer legislation

The protection given to consumers by Finnish insurance legislation is supplemented by consumer protection legislation, which is also applied to voluntary insurance contracts, notably in respect of marketing, contract terms as well as adjustment and interpretation of the contract. In practice this means, for example, that insurers' marketing methods and legality of contract terms are also overseen by the Consumer Ombudsman.

Besides insurance legislation, insurers have to take account of data protection legislation in their operations. Finnish data protection legislation has been harmonised to conform to the EC data protection directive. The most important piece of Finnish data protection legislation is the Personal Data Act, which has been devised in order to ensure that the right to private life and other fundamental rights protecting privacy are protected in all data processing. The relevant supervisory authority is the Data Protection Ombudsman.

Insurance Companies Act

The Insurance Companies Act sets forth provisions governing the incorporation, administration, annual accounts, solvency, investment and supervision of insurance companies. This act is supplemented by decrees and regulations issued by the Ministry of Social Affairs and Health and the Insurance Supervisory Authority.

Before an insurance company can be established, a licence is required from the Ministry of Social Affairs and Health. Unlike the practice in many other countries, the licence requirement also applies to companies specialising in reinsurance alone. A licence is granted if the information received on the business envisaged and on the members of the company gives sufficient grounds to judge that the insurance company will comply with sound and prudent business principles in its operations, providing that the insurance company's management meets the requirements imposed thereon in the act and that the company has sufficient share capital or equivalent funds. The share capital or equivalent funds must amount to a minimum of €3 million in life insurance companies and in non-life insurance companies carrying on motor liability, credit and suretyship, liability or business interruption insurance business and to a minimum of €2 million in non-life insurance companies writing non-life business other than the mentioned classes.

Life insurance and non-life insurance business may not be carried on in the same insurance company: a non-life insurer may write no other than non-life business and a life insurer may write life, accident and health insurance business alone. Nonetheless, although life, non-life and employee pension insurance must be carried on in separate legal companies, such companies often operate in a group of companies or otherwise in close cooperation with each other.

Employee Pension Companies Act

As providers of social insurance, employee pension insurers are considered to differ from other insurers to the extent that they are governed by a separate piece of legislation, which contains provisions applied exclusively to employee pension insurers. Separate legislation has been drafted in order to ensure the independence of authorised employee pension insurers versus other insurance companies in the same group, the company's shareholders and financial institutions.

The Employee Pension Insurance Companies Act regulates ownership of employee pension insurers' assets, the companies' investment and organisation of investment operations and contains provisions on the representation of social partners on the board of directors and the supervisory board of every employee pension insurance company.

Insurance Associations Act

Insurance associations are local mutual insurers whose operations are based on policyholders' joint liability and regulated by the Insurance Associations Act. Local mutuals' geographical reach is limited: one insurer may operate in a territory consisting of up to 40 municipalities. This restriction serves to ensure that the associations retain their local image.

Local mutuals may only engage in voluntary non-life business. Their administration structure is similar to the organisation of mutual insurance companies.

In January 2005, there were 99 local mutual associations operating in the Finnish insurance market. Measured by gross premiums written, local mutuals rank the largest farm insurer in Finland.

Foreign Insurance Companies Act

Finland's membership in the European Union has brought about many changes in legislation governing non-Finnish insurance companies. Many of the changes relate to criteria applied to foreign insurers' entry to the Finnish insurance market, following deregulation of the business. This deregulation applies to insurers registered in other EEA countries, not to insurers registered outside the EEA in so-called third countries. Against this background, the Foreign Insurance Companies Act divides foreign insurance companies into two categories: foreign insurers with a registered office in the European Economic Area (foreign EEA insurers) and foreign insurance companies with a registered office outside the EEA (third-country insurers). The regulations applied to these two categories are very different in many crucial points.

The Foreign Insurance Companies Act does not apply to reinsurance at all, because reinsurance business has always been allowed for foreign insurers in Finland without any consent from or supervision by Finnish authorities.

In accordance with the single licence principle, foreign EEA insurers need no consent from Finnish authorities to establish a branch in Finland or to start doing insurance business in Finland from a presence

abroad under the freedom to provide services. The financial supervision of such insurance companies is in the hands of the relevant authorities of the company's home state.

Criteria for carrying on statutory non-life insurance

If a foreign EEA insurer wants to carry on motor liability insurance business in Finland from a presence abroad under the freedom to provide services, the company must appoint a claims representative in Finland to take charge of the payment of claims to the injured.

The specific laws issued for individual statutory insurance lines impose another obligation on foreign insurers wishing to carry on statutory non-life business in Finland, either motor liability, workers' compensation, patient or environmental impairment insurance, under the right of establishment or the freedom to provide services: they are required to join the central body of the line concerned, ie the Finnish Motor Insurers' Centre, the Patient Insurance Centre, the Environmental Insurance Centre or the Federation of Accident Insurance Institutions. Membership in these bodies is compulsory for not only foreign EEA insurers and third-country insurers but also Finnish insurers.

Obligation to appoint a tax representative

In addition to the above requirements, non-life insurers carrying on business under the freedom to provide services must appoint a tax representative in Finland to collect premium taxes and fire brigade charges. The appointee must be a company with a registered office in Finland and with adequate experience and competence for performing the duties of a tax representative.

Third-country insurers need a licence

Since third-country insurers, ie insurers based outside the EEA area, are not affected by the European integration process or by the single insurance market, they continue to need a licence to do business in Finland. The licence is granted by the Ministry of Social Affairs and Health. To do business in Finland, third-country insurers must establish a branch in the country. The criteria applied to the granting of licence and the regulations governing third-country insurers' business are much the same as the provisions governing Finnish insurers.

In January 2005, there were 21 foreign insurers' branches in Finland. One of the branches was Swiss and the remaining 20 were EEA insurers. More than 400 foreign

insurers had filed a notification of their intention to start business in Finland under the freedom to provide services. Foreign insurers' branches cover a modest share of the Finnish market so far, about 2 per cent in non-life and 4 per cent in life insurance in 2003.

Insurance Mediation Act

The Insurance Mediation Act applies to insurance intermediaries who sell or broker insurance policies or who otherwise prepare or conclude insurance contracts or assist in the administration or performance of such contracts.

Insurance intermediaries are either brokers or agents. Insurance brokers act under their agreement with their customer, independent of all insurers. Agents, instead, act for the account of and under the responsibility of the insurer concerned.

Insurance intermediaries need to be registered with the register of insurance intermediaries kept by the Insurance Supervisory Authority. The criteria to be met by insurance agents to qualify for registration include reliability and sufficient professional skills. Insurance brokers are required not only to have these qualities but also to be independent of the insurer concerned and to hold liability insurance.

An insurance intermediary registered in one member state of the European Economic Area may also operate in any other EEA state. These operations require a notification filed with authorities of the states concerned.

The Insurance Mediation Act also contains provisions on insurance brokers' responsibilities and disclosure requirements.

Insurance intermediaries are supervised by the Insurance Supervisory Authority.

In December 2004, the register of insurance intermediaries kept by the Insurance Supervisory Authority contained 67 insurance broker businesses, which employed a total of 266 registered insurance brokers. In 2003, the volume of premiums written on policies mediated by insurance brokers accounted for 6 per cent of all premiums written in non-life insurance, for 7.1 per cent in life insurance and for 18.4 per cent in statutory employee pension insurance.

Supervision

The operations of insurance companies and other insurance institutions such as pension funds and insurance brokers are supervised by the Insurance Supervisory Authority.

Not unlike many other countries, Finland has seen a debate emerge on many occasions on whether supervision of the whole financial services industry should be built under one single authority. But the debate has always ended in the conclusion that the two supervisory arms be kept apart because of the major differences between banking and insurance, not least the core position of statutory social insurance. Cooperation between the two bodies has, however, been strengthened, particularly in respect of groups comprising insurance companies, credit institutions and other financial services companies. Furthermore, supervision of insurers' operations has been transferred from the Ministry of Social Affairs and Health to the Insurance Supervisory Authority, a separate body independent of the Ministry, whereas legislation remains with the Ministry. One of the main aims of this arrangement is to separate supervision from regulation, ie law drafting and issuance of regulations supplementing the laws, duties which remain with the Ministry of Social Affairs and Health.

The functioning of cooperation between the Insurance Supervisory Authority and the Financial Supervision Authority, which oversees the banking sector, has been

ensured starting from the top: the boards of the two authorities comprise largely the same persons. Exchange of information between the authorities has also been improved.

The principal role of the Insurance Supervisory Authority is to safeguard the interests of insurance customers, and this is where financial supervision takes the centre stage. Secondly, the supervisory authority verifies that companies operate lawfully and comply with good insurance practice. The most vital parts of financial supervision are verification of the adequacy of companies' solvency margins and supervision of investment in assets covering technical provisions. In these two fields, the supervisory body verifies that the companies meet the minimum requirements imposed in EC insurance directives, although in practice Finnish life and non-life insurers' solvency is well above the EU average.

Prudential supervision

Since as early as 1952, Finnish insurers' solvency has been supervised by means of a solvency test. The test incorporates an early warning system, which helps the supervisory authority identify risks early enough and tackle the problem if a company's solvency weakens. In its present form, the solvency test evaluates the nature of insurance business and the underlying risks as well as the

risk content of the company's investments. The concept of solvency capital is wider than the EU concept of solvency margin. Solvency capital includes eg assets valued at current value and possible prudential margins on the liabilities side, such as equalisation provision. Although the solvency test has been designed to reflect individual companies' risk profiles, it is a comparatively simple way to test a company's solvency eg on the basis of figures released in annual accounts.

Non-life insurance is a business particularly susceptible to stochastic fluctuations. To reduce the negative impact of stochastic fluctuations, insurers are required by the Finnish Insurance Companies Act to include in their provision for claims outstanding a specific item, equalisation provision. This provision is used for adjusting the reported profits over a fixed period of time to a level required by the average loss ratio.

This practice has been built to secure insurance companies' claims paying capacity over a very long period. Finnish regulations on insurance supervision, companies' solvency and diversification of investments have been upgraded after two bankruptcies in the early 1990s. In addition, insurers writing statutory business are required to set aside funds for a guarantee scheme to make sure that the insured and claimants receive full compensation and benefits due to them under motor liability, patient, workers' compensation and employee pension insurance,

even if the insurer becomes insolvent. When an insurer becomes insolvent, the other insurers are required to make contributions to the guarantee scheme to cover the amount needed for the payment of compensation and benefits due. The guarantee scheme has not been extended to voluntary life and pension insurance.

The solvency requirements imposed on authorised pension insurers are different from those imposed on other insurers. First, pension insurers' technical provisions include an item headed provision for future bonuses, which has been set up to serve as a buffer against ups and downs in the values of the companies' investment assets. Second, pension insurers' solvency is supervised with the help of supervisory limits set individually for each insurer on the basis of the risk content of its investments.

The near-future challenges faced by prudential supervision are progress of the EU Solvency II Project on the one hand and obligation imposed on some companies to apply the international accounting standards (IAS/IFRS) on the other hand. For the moment this problem has been solved by an arrangement where solvency is supervised on the basis of separate financial statements prepared according to existing national regulations, which means that prudential supervision is not impacted by the international reporting standards.

Cooperation with insurance consumers

Cooperation with insurance consumers

Cooperation with insurance consumers involves authorities, consumer bodies and insurance companies under a contractual consumer organisation set up in the Finnish insurance industry as early as 1971. Based on an agreement between the National Consumer Administration and the Federation of Finnish Insurance Companies, the organisation is made up of three separate bodies: the Finnish Insurance Ombudsman Bureau, the Supervisory Board of the bureau, and the Finnish Insurance Complaints Board. This is one of the oldest arrangements in Europe set up to offer a way other than litigation to solve disputes between insurers and claimants and to produce impartial information for consumers. All parties are very satisfied with the operations of the organisation, as it provides a quick and simple way for consumers to have disputes settled, free of charge, and a forum for discussion on insurance consumer issues.

The role of the Finnish Insurance Ombudsman Bureau is to give guidance and advice to customers and to settle claims disputes. The bureau's remit extends to all voluntary insurance and four statutory lines, patient, workers' compensation, motor liability and environmental impairment insur-

ance. In claims disputes, for example, the bureau negotiates with the insurer on behalf of the customer. If this does not result in an outcome satisfactory to the customer, the customer may refer the case to the Finnish Insurance Complaints Board.

The Finnish Insurance Ombudsman Bureau receives about 8,500 enquiries and complaints a year. On the guidance front, the bureau helps consumers choose their insurance cover by making comparative studies of insurance products and prices, which are available on the bureau's web site at www.vakuutusneuvonta.fi. If any problems come up in connection with the advisory work, the problems are reported to insurance companies.

The Finnish Insurance Complaints Board processes complaints made by policyholders, insured persons, injured parties, beneficiaries and insurance companies. Not only consumers but also businesses may ask for a statement from the board, which deals with all voluntary lines of insurance. Although the board's statements serve as mere recommendations, insurers usually comply with them.

The Complaints Board settles about 800 complaints annually. Roughly one third of the cases processed end up in favour of the customer.

The Supervisory Board of the Finnish Insurance Ombudsman Bureau serves as an administrative body that steers and supervises the operations of both the bureau and the Finnish Insurance Complaints Board and appoints the members of the Complaints Board. The Supervisory Board also issues opinions and gives statements on questions of principle or other issues of importance to the insurance industry. The Supervisory Board is chaired by the director general of the Insurance Supervisory Authority, and half of its members represent consumer authorities and organisations, while the other half come from insurance companies. The Complaints Board has the same composition. The chairmen of the committees operating under the Complaints Board are impartial, the present chairmen being university professors.

Work within the EU has resulted in the creation of an EEA-wide out-of-court scheme, FIN-NET, for solving cross-border disputes in the financial industry. FIN-NET is a cooperation network for consumer disputes in insurance, banking and investment and the scheme is made up of dispute settlement bodies operating in the countries concerned. Both the Finnish Insurance Ombudsman Bureau and the Finnish Insurance Complaints Board are members of FIN-NET. Active since 2001, FIN-NET was devised to make it easier for consumers to communicate with dispute settlement bodies in other countries. So far there have not been many cross-border insurance disputes.

Cooperation within the industry

The insurance industry is involved in cooperation on many fronts through its lobbying bodies and a number of statutory entities.

Federation of Finnish Insurance Companies is a lobbying and cooperation body for insurance companies operating in Finland. The Federation's goal is to create welfare by means of insurance by working as a trusted influencer in society. The Federation is a member of the Confederation of Finnish Industries.

The Finnish Motor Insurers' Centre is a cooperation body for motor liability insurers operating in Finland. Moreover, the Centre serves as a Green Card bureau communicating with its counterparts abroad in matters handled under the scheme. Apart from insurance, the Centre is involved in extensive road safety development work and maintains the operations of road accident investigation teams.

Federation of Accident Insurance Institutions is the central body for workers compensation insurance in Finland. Its main role is to coordinate implementation of this statutory line of insurance. All insurers writing workers compensation insurance in Finland have to be members of the Federation.

Finnish Pension Alliance TELA is a lobbying body and a service entity for authorised pension insurers providing statutory pension cover to employees in both the private and the public sector. As a repre-

sentative of its members, TELA works to secure employee pensions, to upgrade the scheme and to make the system known to the public.

Finnish Centre for Pensions is the central body for the Finnish scheme of statutory employee pensions and a specialist in employee pension provision. Its role is to secure uniformity of pension provision in Finland and to provide services to both the insured employees and their employers.

Insurers' social responsibility

Social responsibility in the insurance industry translates into responsible involvement in social welfare provision beyond legislation and regulation. Shouldering social responsibility is up to the insurers themselves; they are free to choose the forms of involvement individually.

Together with representatives of its members, the Federation crafted a discussion paper on social responsibility in the insurance industry in 2002 to help individual insurers build their own social responsibility framework.

Owing to the nature of insurance business, insurers' social responsibility involvement is marked by economic responsibility above all, though all aspects of social responsibility are present in the efforts. Devising ways to measure social responsibility involvement and to report on companies' performance on this front poses a major challenge to Finnish insurers at this point.