УДК 336.2

RISK MANAGEMENT IN INSURANCE COMPANIES OF CHINA

Li Yanlong, Master Student,
Pryhodzich Iryna, PhD in Economics, Associate Professor,
Polessky State University, prigodich.i@polessu.by

Annotation. The article contains information about the nature and methods of risk management in insurance companies. The main goals and directions of risk management development in China are considered. The main advantages and disadvantages in the studied issue in insurance activity are determined.

Keywords: risk, insurance activity, assessment, control, insurance market.

According to Swiss Sigma statistics, 648 insurance companies went bankrupt in the world from 1978 to 1994, especially from 1996 to 2001, seven consecutive life insurance companies in Japan with highly developed insurance industry went bankrupt. In

China, Standard & Poor's assessment of China's insurance industry risk in China Insurance Industry Credit Outlook 2006-2007 is that the industry risk of both life insurance and non-life insurance is still relatively high. This has sounded the alarm for China's insurance industry: insurance companies must strengthen their own risk management while operating risk products. The brand-new risk management concept and technology put forward by the enterprise risk management framework issued by COSO of the American Anti-Fraud Financial Reporting Committee has great theoretical and practical significance for the risk management of insurance enterprises in China.

First, the necessity and importance of implementing comprehensive risk management in insurance enterprises

Risk management of insurance companies is an eternal topic. Focusing on the overall business objectives, insurance companies can cultivate a good risk management culture and establish a comprehensive risk management system by implementing the basic processes of risk management in all aspects and processes of enterprise management, which can play an important role in preventing and defusing risks, protecting the safety and integrity of assets, ensuring the legal compliance of business activities and the effective implementation of business strategies:

1) the trend of insurance internationalization is increasingly obvious.

Under the background of economic globalization, the trend of insurance internationalization is becoming more and more obvious. On the one hand, it shows the globalization of customers' insurance needs, and multinational companies arrange their risk management and insurance plans around the world based on their global operations. On the other hand, insurers meet the rapidly growing needs of catastrophe insurance and financial risk management through international insurance capital operation, hedging mechanism and strategic alliance, and seek new living and development space in the international scope. Self-insurance companies in the true sense appeared in 1960s, banking insurance initiated by the Dutch in 1970s and quickly swept the world, product innovations represented by universal life insurance and variable life insurance in 1980s, insurance risk securitization and a large number of new risk transfer tools in 1990s, especially in recent years, insurers, insurance brokers, government insurance institutions and non-governmental insurance organizations, such as Allianz Insurance. A lot of innovations have been made in new insurance products and technologies, such as Integrate Risk Management and Alternative Risk Transfers. The scope of insurance protection has greatly broken through the traditional insurable risk category, which indicates revolutionary changes in the insurance industry in the future.

2) insurance funds are facing increasing investment risks.

With the innovation and integration of financial market, the channels of insurance funds are gradually expanded, and the investable varieties are gradually increased. From ordinary bond investment to equity investment, from domestic market to overseas market, the risks faced by insurance funds, especially life insurance funds, are becoming more and more complex. For example, life insurance policies generally last as long as 20 to 30 years, and corresponding investments with a duration of 20 to 30 years should be considered to match them in the use of funds. Life insurance funds invested in fixed income assets are very sensitive to changes in interest rates, and small fluctuations in market interest rates will lead to large changes in asset values. According to statistics, by August 2006, bonds had become the most important tool for the allocation of insurance assets, and the investment scale had reached 877,7 billion yuan, of which the balance of holding national debt and financial debt reached 367,4 billion yuan and 241,6 billion yuan respectively. The proportion of bond assets in the use of insurance assets increased from 28,4 % in 2001 to 55,2 % in 2006, Corporate bonds, bank subordinated bonds and national debt held by insurance companies. Under the background that the central bank raises interest rate and the yield of bonds such as national debt drops sharply, the investment risk of insurance companies is obviously increasing. The low investment benefit directly affects the solvency and stability of insurance companies. It is estimated that insurance policies before 1999 will lead to an annual increase of about 2 billion yuan in the spread loss of life insurance industry in China. By the end of 2004, the total spread loss of life insurance industry exceeded 72 billion yuan, accounting for about 9% of the total assets of the industry. Even if all the business surpluses of life insurance companies are used to make up for the spread loss, it will take 10 years to resolve it. However, equity investment, including financial derivatives investment, has a huge risk, which brings hundreds of millions or even billions of losses to many companies, such as German Gotha Insurance Company, Cronia Insurance Company, Hannover Reinsurance Co., Ltd, and Bahrain Bank of London, etc. Therefore, it is very important to strengthen the risk management of capital utilization and improve the level of risk management.

3) comprehensive risk management has become the foundation and core of modern insurance enterprise management.

With the deepening and expansion of the financial and insurance market, the competition among insurance institutions has gradually changed from the original scale expansion to the competition in internal management and business innovation, which has led to profound changes in the business philosophy of insurance enterprises, and made comprehensive risk management the foundation and core of modern insurance enterprise management. From a global perspective, risk management is moving from the traditional "point-to-point" management to comprehensive and integrated management. Internationally famous internal control and risk management models include Cadbury in Britain, COSO in the United States and COCO in Canada, especially COSO in the United States, which expounds a complete and comprehensive enterprise risk management framework from theory to operation method. William J. Mc·Donoush said, "Internal control will play an important role in protecting investors, because stable internal control is the first line of protection against misconduct and the most effective preventive measure to deter fraud". In 2005, China Insurance Regulatory Commission formulated the Measures for Internal Control Evaluation of Life Insurance Companies (Trial). In 2006, the State-owned Assets Supervision and Administration Commission formulated the Guidelines for Comprehensive Risk Management of Central Enterprises. This is of great significance to promote the development of comprehensive risk management of insurance enterprises.

4) China's insurance industry has many shortcomings in risk management.

In recent years, with the rapid development of domestic insurance industry, some progress has been made in preventing and defusing operational risks and enhancing internal risk management, but there are still many problems and deficiencies, which are mainly manifested in three aspects: First, the understanding of comprehensive risk management is not in place, and there is a serious "shaft effect". Second, there is no complete risk management framework. The risk management of most insurance companies has not been implemented in all business processes and operation links of the company. Many key control points have formed so-called control blind spots, and an effective multi-dimensional, multi-perspective and cross-time risk monitoring system has not yet been formed. Third, the effect of risk management is not satisfactory, and there are many violations of laws and regulations. Therefore, only by introducing, digesting and absorbing the international advanced enterprise risk management mode and risk management technology from the reality of Chinese insurance companies, especially making the COSO framework the standard for insurance companies to improve their internal control, constructing a comprehensive risk management system, and narrowing the gap between our risk management and the international ones, can the insurance industry resist risks and develop stably and healthily.

At present, there are many internal control and risk management standards in the field of international risk management, but they are all closely related to COSO framework, which has become the standard of enterprise comprehensive risk management. Therefore, in order to improve the internal control of insurance companies and enhance risk management, it is necessary to accurately understand the connotation of enterprise risk management framework defined by COSO, and establish insurance company risk management framework and mechanism based on COSO framework to win the trust of investors and enhance the reputation of insurance companies in the public.

As early as 1958, American Institute of Certified Public Accountants divided ”internal control“ into two categories: internal accounting control and internal management control. In 1992, COSO put forward the overall framework of internal control, which was supplemented in 1994, pointing out that internal control is to achieve the effect and efficiency of operation. The process of complying with the three goals of current laws and regulations. In October 2004, COSO officially released the enterprise risk management framework (hereinafter referred to as ERM framework). On the basis of the report in 1992, ERM framework absorbed the research results of risk management in various aspects, and made extended research, and put forward the risk management idea of combining internal control framework with enterprise risk management [1].

COSO’s definition of ERM framework is that ”enterprise risk management is a process, which is implemented by the board of directors, management authorities and other personnel of a subject, applied to strategy formulation and runs through the enterprise, aiming at identifying potential issues that may affect the subject, managing risks to make them within the risk capacity of the subject, and providing reasonable guarantee for the realization of the subject's objectives“. COSO’s risk management framework expands its internal control framework, emphasizing that enterprise risk management has three dimensions, namely, objectives, risk management elements and management levels. The objectives are expanded from 3 to 4 in the internal control framework, namely, strategy, operation, reporting and compliance. The risk management elements are expanded from 5 (internal environment, risk assessment, control activities, information and communication, monitoring) to 8, namely, internal environment, target setting, event identification, risk assessment, risk response, control activities, information and communication, monitoring. The management level includes the whole enterprise, functional departments, business units and branches. Each management level is the main body of risk management, the elements of risk management are the necessary conditions, and the objectives are the objects that enterprises strive to achieve. All management levels of enterprises should serve four objectives according to the eight elements of risk management.

COSO began to study enterprise risk management in 2001, emphasizing that the risk management framework must be consistent with the internal control framework, and integrating the internal control objectives and elements into the overall risk management process of enterprises. Therefore, ERM framework is an extension of internal control framework, which covers internal control and is more complete and effective than internal control. First of all, the framework expands the internal control framework, emphasizing the coordination between risk management and corporate strategic objectives, and finally integrates into corporate culture; Secondly, the framework emphasizes that risk management runs through all aspects of the enterprise operation process, involving all levels of enterprise governance, management and operation, and expands the simple internal control function; Finally, new research results of risk management theory, such as risk combination, risk and opportunity distinction, risk response, risk preference and risk capacity, are introduced. ERM framework is an important development of traditional risk management and internal control, it has a clear cultural concept, a complete architecture system, a scientific control process, and effective technologies and methods, it can cover all kinds of risks of enterprises and manage them comprehensively. Therefore, the application of this framework is of great significance for China's insurance enterprises to effectively implement risk management and comply with the risk control and regulatory requirements of regulatory agencies [1].

Comprehensive risk management is a brand-new management concept and method, China's insurance industry must change its long-standing concept and mindset as soon as possible, and strive to build a new system and mechanism of comprehensive risk management. ERM framework emphasizes that determining whether a subject's enterprise risk management is ”effective“ is a judgment made on the basis of evaluating whether eight components exist and operate effectively, if the components exist and operate normally, there may be no major defects, and the risk may have been controlled within the scope of the subject's risk capacity:

1) the internal environment;
2) goal setting;
3) risk identification and risk assessment;
4) risk response;
5) control activities;
6) information communication;
7) monitoring;
8) individual evaluation.

The multi-directional and three-dimensional risk management and monitoring system thus established will build a solid barrier for insurance companies to standardize their operations and prevent and resolve risks.

COSO's enterprise risk management framework is based on the multi-dimensional, three-dimensional and continuous characteristics of risk management. It emphasizes that insurance companies have a comprehensive and in-depth understanding of control and control objects, analyze and solve complex problems existing in management control, manage the company's liabilities, investment, interest rates and other risks as a whole, and establish a direct link between risk management and Shareholder Value Maximization, providing a strict and feasible management framework for insurance companies' risk management.

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