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# **DEVELOPMENT OF MUTUAL INSURANCE IN RUSSIA BASED ON SOCIAL ECONOMY IDEA**

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### *Abstract*

One of the problems of the Russian insurance market is the distrust of the population towards commercial insurance companies. With poor financial literacy, citizens often cannot get the level of insurance they wanted. In addition, the high cost of policies at low incomes of the population and small businesses scares away potential insurers. Mutual insurance could be the method of creating an insurance product that would reconcile the insured with its financial capabilities. By developing mutual insurance as a type of social entrepreneurship, the State can achieve certain results not in protecting the population from risks only, but also in increasing the level of financial literacy of the population. This will have an impact on the financial market as a whole. The purpose of the article is to justify the potential possibility of a new direction of development of the insurance market of Russia based on stimulation of the activities of mutual insurance societies. The specific nature of the business model of mutual insurance meets the psychological needs of citizens: protection, solidarity, mutual assistance and equal democratic participation in governance. However, the state has to recognize the importance of this direction and pay sufficient attention to ensuring the financial sustainability of mutual insurance societies. The development of mutual insurance as a type of social entrepreneurship will reverse citizens "mistrust of insurance. In addition, it will provide citizens with insurance services at a fair price and according to their needs.

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**Keywords:** Mutual insurance, social economy, social entrepreneurship.



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## 1. Introduction

The Russian Federation is in a "new economic reality," which is characterized by a decline in the standard of living of the population, a decrease in the capacity of the State to implement the tasks of social policy, problems in the financial market, including in the sphere of insurance (Maslennikov & Maslennikova, 2017). A developed insurance market is an integral characteristic of countries that have achieved economic prosperity. As is known, insurance in economics performs many important functions. Of particular note, it is an important element of the social protection system, ultimately benefiting human capital and reducing existing inequalities (Maslennikov & Maslennikova, 2017). Russian insurance market was going through a stage of stagnation, despite a visible increase in insurance premiums. At the same time, the number of insurance companies is reduced by 9 % after active cleaning of the insurance market by the mega-regulator (Statistical indicators and information on individual insurance entities, 2018). According to the results of 2017, the level of penetration of life insurance in Russia is 0.4 %, on average worldwide – 3.5 % of GDP. In the non-life segment (insurance other than life insurance), the lag is less noticeable, but also significant. According to the results of 2017, the ratio of insurance premium to GDP was about 1 %. The global average is 2.8 % of GDP (Bredichin, Sharapov, & Porakhova, 2019).

The potential insurer in the search for the best service at the optimal price turns to other methods of creating an insurance product. Mutual insurance is such a method. With the arrival of the global crisis, the situation of the European insurance market has changed. European mutual and cooperative insurance companies reported rising premium revenues at a much greater rate, than the rest of the European insurance market. This reflects the desire of insurers for the quality and safety of services provided by mutual insurance societies in conditions of deep economic instability.

In conditions of complete mistrust of consumers to the financial market of Russia and reduction of incomes of the population, the development of mutual insurance can be a response to the consumer 's request for an affordable and quality service. The idea of a social economy and a non-profit approach give impetus to the development of mutual insurance, which is based on solidarity and democratic governance.

The emergence of the term "social economy" reinforced the relevance of mutual insurance. Social entrepreneurship in modern society involves an altruistic manner of doing business focused on public benefits. The mutual insurance communities were thus competitive, based on solidarity that went beyond the limits of the market and extended to social reality.

## 2. Problem Statement

In the context of the economic crisis, insurance companies faced financial instability, falling demand for insurance products. In the search for ways to increase sales, insurers seek to optimize insurance rates, develop new approaches to customer retention, develop sales channels (Bredichin, Sharapov, & Porakhova, 2019; Brovkin & Khorin, 2018a; Khitrova, 2016).

However, having analysed the views of consumers on the potential of the insurance market, we see, first of all, a high degree of distrust of the population towards commercial insurance companies, second, a high cost of insurance products, and third, a decline of consumer incomes (Gorulev, 2019; Overview of the

insurance market in Russia, 2019). Today, the insurer wants to receive a service at a fair price, taking into account his real needs and with possible control over the insurance fund.

Mutual insurance is by its very nature the most equitable method of organizing an insurance fund and meets the basic needs of potential insured persons. In foreign practice, mutual insurance was formed at the initiative of the insured themselves, as they realize the need for insurance protection. In mutual insurance, participants actively participate in the development of strategy of the mutual insurance society and discuss all important legal issues. Such participation has a positive socio-psychological dimension. Thus, mutual insurance becomes a form of economic self-organization of the population. That was what was reflected in the phenomenon of social economy.

Until the mid-twentieth century, economists and politicians had not seriously considered the idea of mutual insurance. This form of insurance relations was actively used primarily in social insurance and social insurance. Mutual insurance has become the basis for the creation and development of compulsory social insurance (Hamitov, 2015; Orlanyuk-Malitskaya, 2015).

Currently, mutual insurance occupies 16 % of the European insurance market, it collects 180 billion Euros. About 230 million citizens are insurers. More than 200.000 people work in mutual insurance societies. The decision of many insurers to turn to mutual insurance to insure their needs in the face of an economic downturn is an indicator of confidence in good reputation. The ability of mutual insurers to respond quickly to external factors and regulatory demands was recognized as unique and would play a major role in their future success.

The question arose – was it possible in the Russian insurance market to obtain the same presence of mutual insurance as in Europe? Are Russian citizens ready to actively use insurance services to join mutual insurance societies?

In modern Russia, mutual insurance does not develop. At the same time, everyone recognizes the obvious advantages of this form in protecting the rights and interests of consumers of the insurance service compared to the commercial form. And it 's a social problem, but not an economic one. If in developed economies (as in Russia of the early 20th century) a potential consumer of understands the need for mutual insurance service, in modern Russia there is no one. Neither citizens nor enterprises are willing to cover each other's risks based on reciprocity. The origins of this perception of mutual insurance are of a socio-psychological rather than economic nature, and lie in the loss of confidence in any financial assets and market entities (Stepanova, 2017b).

### **3. Research Questions**

Among the main issues raised in this work are the following ones: 1) the disclosure of the role of the social economy in the European context; 2) Development of mutual insurance as a subject of social economy; 3) Opportunities to stimulate the development of mutual insurance in the Russian insurance market in the context of the social economy.

#### **4. Purpose of the Study**

The research purpose is to determine the possibility of stimulating the development of mutual insurance in the Russian insurance market based on the active introduction of the idea of social economy, which could eventually lead to greater efficiency and social justice in the market, taking into account the interests of consumers in the first place.

#### **5. Research Methods**

Investigation method: (1) problem definition, (2) formulation of our original hypothesis, (3) search for primary studies, (4) analysis and synthesis of relevant data, and (6) analysis of hypothesis confirmation and formulation of conclusions.

#### **6. Findings**

The social economy is not a new concept for Russian reality. But in studying this term, researchers note that there are different approaches to the content of the term "social economy" (Bagdasaryan & Sochneva, 2016). Traditionally, the social economy includes non-profit enterprises and organizations, enterprises based on solidarity and non-profit. The term "social economy" was first used in the scholarly work of the French economist Charles Dunuaye (1830), in which he defended the ethical approach to economics (as cited in Sánchez, 2010). The social economy (according to the definition given at the Congress of CEPES (Spanish Business Confidence of the Social Economy)) is any economic activity based on people, who working in democratic cooperation in joint ventures, and which gives priority to the personal contribution of people and their work, rather than profit or capital development (Ruano & Manso, 2019). The Commission of the European Union determined in 1989, that enterprises of the social economy are those, whose economic activities are carried out in specific organizational structures. These structures or methods of organization are based on the principles of solidarity and participation in governance (usually "one person, one vote") of their members, whether producers or consumers, and on the values of autonomy and citizenship development (Ruano & Manso, 2019). For the most part, these enterprises take the legal form of cooperatives, mutual societies or associations.

Social entrepreneurship is the use of entrepreneurship tools to develop, finance and implement solutions to social, cultural or environmental problems. In the European Union, social entrepreneurs, building on the strengths of the long-standing social economy tradition, have become agents of change and actively participate in the development and implementation of innovative solutions to major economic and social problems at present.

In the European Union countries, the idea of developing common approaches in the legislative framework regulating the activities of social economy actors has recently been actively promoted. The institutions of the European Union stressed the relevance and need to promote social economy in its economic and legislative sphere as an instrument of territorial development (Ruano & Manso, 2019). The social economy contributes further to several key European Union goals, including achieving sustainable and inclusive growth, high quality employment, social cohesion, social innovation, local and regional

development, and environmental protection. In addition, an important tool contributes to the growth of well-being.

At the same time, social economy is a sector that has experienced a better economic crisis, than others have. Social economy is becoming increasingly recognized at the European level (The promotion of the social economy..., 2015).

At 2015 report by the European Parliament notes that mutual insurance societies, along with other social economy enterprises, play a significant role in the European economy, especially during the crisis. They protect against loss, create jobs, while forming economic and social cohesion among economic actors.

Economic and social shifts over the past decade have created a substantially different type of insurance consumer. The global financial crisis has led to a drop in real terms and a slowdown in commercial activity in many markets. Consumer sensitivity to prices has increased and their expectations for services continue to rise. Mutual insurance societies, as subjects of social entrepreneurship, can become one of the directions of its development in the Russian insurance market, as well as meet the needs of insure in new economic realities.

Mutual insurance societies, like all social entrepreneurs, use most of their possible income as a means to achieve their core social goals rather than maximizing profits for their owners. The insurance fund is jointly owned by all members. The insurers have obligations to manage this fund and to use the fund, including on mutual payment of damage at the end of the year.

Mutual insurance societies provide "fair" conditions on insurance contributions and payments to their members, and the possibility of spending funds accumulated in the societies to finance preventive measures. (Burkov, 2001). The business model of mutual and cooperative insurance focuses on the use of surplus exclusively for the benefit of insured members and society. This is the original form of insurance and is a more natural choice, than modern widespread shareholder-driven model.

Mutual and cooperative insurance is present in almost all markets in Europe, established there or (mainly in Central and Eastern European countries) through subsidiaries of foreign mutual companies.

The historical past of Russia is the richest moneybox of practical experience both of the organization of mutual insurance and of its successful functioning. In pre-capitalist Russia, the most common form of insurance was mutual insurance assistance, i.e. members of a collective insured each other free of charge, without benefit (did not set the purpose of income generation). In the Russian Empire, with its multi-dimensional, significant patriarchal nature of public production, mutual insurance played a prominent role. The largest economic "power" was achieved by mutual insurance societies created on their own initiative by the insured. Thus, at the end of the 19th century societies of mutual insurance in Russia began to be actively formed in the production sphere on a professional basis (Brovkin & Khorin, 2018b; Orlanyuk-Malitskaya, 2015).

The analysis of the Russian insurance market shows that with all its advantages, mutual insurance did not find a response from consumers of insurance services. During the period 2014–2018, the number of mutual insurance societies remained almost unchanged: 11–13. The total number of members of such societies is 1,173. By comparison, the number of commercial insurance companies decreased from 400 to 177 (Statistical indicators and information on individual insurance entities, 2018).

The main reason, in our opinion, is the lack of public confidence in such a method of organizing an insurance product and weak financial literacy. Due to the peculiarities of the Russian mentality, the population does not trust financial institutions, whose activities are not subject to strict and close supervision by the state.

Turbina and Dadkov (2007) note that "normative and legal acts regulating key provisions of society activities" are the foundation on which "all societies of mutual insurance activities" in the world are based. The main elements of insurance supervision worldwide are licensing of mutual societies and control of their solvency (Brovkin & Khorin, 2018a,b). In accordance with Russian legislation, mutual insurance companies in our country are subject to mandatory licensing, but in a simplified manner. Control over solvency is limited, first of all, by control over the state of insurance reserves (Stepanova, 2017a). However, there is no very important, in our opinion, mechanism for controlling solvency and ensuring financial stability – there are no requirements for the size of own funds, including the availability of a guarantee fund. Such a mechanism is mandatory in European practice. Thus, the most important legislative project for the insurance industry in Europe is Solvency II – the main work of European institutions to update the legal framework for the industry. The main objective of this structure is to ensure that insurance organizations are financially sustainable and able to withstand adverse events in order to protect the insured and the stability of the financial system as a whole. As Hamitov (2015) rightly notes, a big problem for Russian mutual insurance societies is the initial accumulation of the insurance fund of the necessary volumes. Modern research, both in our country and abroad, describes the funds that have been formed. At the moment, there is little research on the process of establishing mutual insurance societies at an early stage and the problems of transition to a stable state in modern conditions (Hamitov, 2015). Of course, there are other factors that impede the development of mutual insurance in Russia, which are described in the works of other authors (Logvinova, 2016; Orlanyuk-Malitskaya, 2015; Shirshov, 2019; Zhigas, 2014). We believe that special attention should be paid to the issues of capacity to pay and financial sustainability.

The promotion of mutual insurance as a type of social entrepreneurship can give impetus to the development of mutual insurance in order to meet the needs of the population within certain professional or territorial boundaries. Today social entrepreneurship in Russia is especially relevant, because it can serve as a kind of therapy for our society, in which, for a number of reasons, dependency sentiment is strong. While the public and private sectors are engaged in counteraction and competition, when the financing of social programmes and projects is reduced, prices are rising; it is social entrepreneurship that can create stable economic opportunities to solve a number of economic and social problems (Galkin, 2016).

Among the main problems, faced by social entrepreneurship, are the following (Bakhmatova, 2014):

- low assessment of opportunities for solving social problems through social entrepreneurship;
- weak trust of the population
- lack of interest of regional authorities in solving social problems through social entrepreneurship.

By increasing people's interest in mutual insurance, as a form of social entrepreneurship, it is possible to draw the attention of the State to the problem of controlling the solvency of these societies, which means that the degree of confidence in them will become even greater.

The State faces an important task – to create all necessary conditions for the development of social entrepreneurship. With a certain degree of confidence, it can be assumed that, against this background, mutual insurance societies can also develop.

## 7. Conclusion

Russian insurance market is in a period of stagnation. Therefore, the search for ways to revitalize it is actively under way. This takes place against the background of increasing consumer interests in obtaining a service at fair value and high quality. In Russia, mutual insurance has never been considered as a type of social entrepreneurship. At the same time, various types of social entrepreneurship are being intensified in Russia, as people no longer want to be a source of enrichment of private entrepreneurs. Mutual insurance has every chance of active distribution, but under one condition: strengthening control over the state of solvency of mutual insurance companies. Solidarity and reciprocity, joint management and transparency are the main characteristics that can attract potential insurers in Russia. This form of interaction is very close to Russian people and their psychology.

However, it is important to remember that citizens strongly believe in the protection of the state. Russian citizens do not trust financial institutions, which are not closely monitored by the state. A legislative framework should be developed, taking into account European experience in ensuring the financial sustainability of mutual insurance societies. The analysis of Solvency II, a unified approach to ensuring the financial sustainability of the insurance industry, including mutual insurance societies, is interesting.

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