

**Insurance Regulation in the General  
Agreement on Trade in Services: A Model for  
Liberalisation and Development in Nigeria**

**Thesis submitted for the degree of  
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**by**

**Yeside Abiodun Oyetayo  
Bsc, MA,  
ACII MSc,  
LLB, BL  
Faculty of Law  
University of Leicester**

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## **DEDICATION**

**To Dipo, Ayo and Fiyin my most precious gifts from God.**

## ABSTRACT

This thesis argues that the potential for the development of the Nigerian economy could be enhanced through reforms and unilateral liberalisation of the insurance market using the WTO/GATS model before further locked in commitments.

The argument is premised on the analyses of the socio-economic functions of insurance in providing financial stability and welfare for the society and the developmental opportunities within the liberalisation framework of the WTO/GATS as opposed to other alternatives such as regional or bilateral integration. First, the framework serves as a regulatory model on which reforms could be based for efficiency, competitiveness, development and growth. Secondly, it provides a multilateral trading platform guided by trade enhancing rules and principles of the WTO, combined with GATS bottom up approach, progressive liberalisation and technical assistance to developing countries for greater participation in negotiations.

Using the doctrinal analysis and the social science survey technique, this study demonstrates that the legislative and supervisory framework of the Nigerian insurance industry is currently inadequate to provide the growth functions. The problems include structural challenges such as low capacity due to small size of firms, obsolete products and unproductive business processes, unethical practices and a supervisory agency lacking adequate resources, powers, and independence. Others are the restrictive trade practices hindering foreign participation coupled with low insurance awareness and penetration.

The thesis recommends reforms using the GATS model aimed at streamlining the laws particularly with regards to foreign insurers' participation and the adoption of a bi-polar system of supervision to meet the current capacity inadequacies of NAICOM. The adoption of risk based regimes and principled based regulation is also recommended before further locked in commitments which would enhance growth and development.

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## LIST OF ABBREVIATIONS

### WORDS AND PHRASES

African Union	AU
African Economic Research Consortium	AERC
Annex on Financial Services	AFS
American Enterprise Institute	AEI
Authorization and Policy Directorate	A&P
Autonomous Foreign Exchange Market	AFEM
Cambridge University Press	CUP
Central Bank of Nigeria	CBN
Certificate of Capital Importation	CCI
Chartered Insurance Institute of Nigeria	CIIN
Companies and Allied Matters Act	CAMA
Corporate Affairs Commission	CAC
Debt Conversion Committee	DCC
Doha Development Agenda	DDA
Editor/Editors	ed/eds
Economic and Financial Crimes Commission	EFCC
Economic Community of West African States	ECOWAS
Economic Research and Statistics Division	ERSD
Edition	edn
European Union	EU
Footnotes	n

For Example	eg
Foreign Direct Investment	FDI
Forum on Debt and Development	FONDAD
General Agreement on Trade and Tariff	GATT
General Agreement on Trade in Services	GATS
General System of Preferences	GSP
Gross Domestic Product	GDP
Independent Corrupt Practices Commission	ICPC
Insurance Act	IA
Insurance Core Principle	ICP
Ibidem/ same place	ibid
International Association of Insurance supervisors	IAIS
International Development Research Centre	IDRC
International Monetary Fund	IMF
International Trade Organization	ITO
Less Developed Countries	LDC
Massachusetts Institute of Technology	MIT
Most Favoured Nation	MFN
Multilateral Trade System	MTS
National Agricultural Insurance Corporation	NAIC
National Bureau of Economic Research	NBER
National Insurance Commission	NAICOM
National Insurance Corporation	NICON
National Treatment	NT
New Partnership for Africa's Development	NEPAD

Nigerian Financial Sector	NFS
Nigerian Immigration Service	NIS
Nigerian Insurance Industry	NII
Nigerian Investment Promotion Council	NIPC
Nigerian Pension Commission	NPC
Nigerian Reinsurance Corporation	Nigerian Re
One Stop Investment Centre	OSIC
One Stop Services	OSS
Organization for African Unity	OAU
Organization for Economic Cooperation and Development	OECD
Oxford University Press	OUP
Paragraph/Paragraphs	Para/paras
Pension Act 2004	PA
Pension Fund Administrator	PFA
Pension Fund Custodian	PFC
Personal Lines in Insurance	PLI
Principles Based Regulation	PBR
Public Liability Company	PLC
Preferential Trade Agreements	PTA
Publishing/Publications	Pub
Regional Trade Agreements	RTA
Risk Based Capital	RBC
Risk Based Regulations	RBR
Section	s
Securities and Exchange Commission	SEC

Special and Differential Treatment	SDT
Staff Working Paper	SWP
Subject to Regularization	STR
Swiss Reinsurance Company	Swiss Re
Volume/Volumes	vol/vols
United Kingdom	UK
United Nations	UN
United Nations Conference on Trade and Development	UNCTAD
United Nations Department of Economic and Social Affairs	UNDESA
United States of America	USA
University Press	UP
Working Paper	WP
World Institute Development Economics Research	WIDER
World Trade Organization	WTO
<b>JOURNALS</b>	
American Journal of Economics and Sociology	AJES
American Journal of Comparative Law	AMJCL
American Journal of International Law	AJIL
European Business Organization Law Review	EBOR
European Journal of International Law	EJIL
The Geneva Papers on Risk and Insurance	GPRI
International and Comparative Law Quarterly	ICLQ
International Journal of Academic Research	IJAR
International Insurance Law Review	INTILR
International Trade Law and Regulation	Int. TLR
Journal of Financial Economics	JFE

Journal of Insurance Regulation	JIR
Journal of International Banking Law and Regulation	JIBLR
Journal of International Economic Law	JIEL
Journal of Risk and Insurance	JRI
Journal of World Trade	JWT
Minnesota Law Review	Minn L R
Texas Law Review	TLR
The Journal of Insurance	TJI
Third World Quarterly	TWQ
Trade Policy Review	TPR
World Trade Review	WTR

## INTRODUCTION

Economic growth is the most powerful instrument of poverty reduction<sup>1</sup>. However, igniting economic growth and sustaining it require a range of reforms and constructing institutions that can provide resilience from shocks to the economy<sup>2</sup>. The insurance sector is an infrastructural pillar of the economy which supports economic growth and performs tremendous social and economic functions for the society<sup>3</sup>. However, this is only achievable under legal and institutional conditions such as a competitive environment, minimally intrusive and prudent regulations together with a strong regulatory and supervisory body which ensures effective administration and fair competition within the market<sup>4</sup>.

Nigeria is a developing country with abundant human and natural resources. It is also an active member of sub-regional, regional and global trade organizations. Its economic statistics neither reflect its resources nor its participation in these

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<sup>1</sup> Dani Rodrik, 'One Economics Many Recipes: Globalization, Institutions, and Economic Growth' (Princeton University Press, 2009) 2.

<sup>2</sup> *ibid* 16.

<sup>3</sup> Mina Mashayeki, Elisabeth Tuerk and Deepali Fernandez, 'Trade and Development Aspects of Insurance Services and Regulatory Frameworks', in *Trade and Development Aspects of Insurance Services and Regulatory Framework*, UNCTAD/DITC/TNCD/2007/4, 5 <[http://www.unctad.org/en/docs/ditctncd20074\\_en.pdf](http://www.unctad.org/en/docs/ditctncd20074_en.pdf) > accessed 23<sup>rd</sup> April 2011; UNCTAD, 'Report of the Ad Hoc Expert Meeting on Insurance Services' (2006) UNCTAD/DITC/TNCD/2006/1, para 4 <[http://www.unctad.org/en/docs/ditctncd20061\\_en.pdf](http://www.unctad.org/en/docs/ditctncd20061_en.pdf) > accessed 23<sup>rd</sup> April 2011; Konan, D & Maskus, K. (2004), Quantifying the Impact of Service Liberalization In a Developing Country, World Bank Research WP 3913 <<http://elibrary.worldbank.org/docserver/download/3193.pdf?expires=1304834335&id=id&accname=guest&checksum=698DCA9624ECAB3FEC3F117E7E77A087> > accessed 10<sup>th</sup> April 2011; Pierre Sauvé, 'Completing the GATS Framework: Addressing Uruguay Round Leftovers' *Aussenwirtschaft*, 57. Jahrgang (2002), Heft III, Zürich: Rüegger, S. 321 <http://www.cid.harvard.edu/cidtrade/papers/sauve/GATSLeftovers21.doc> 23<sup>rd</sup> April 2011; Marijana Cuak, Sandra Loncar and Klime Poposki, 'Insurance Sector Development and Economic Growth in Transition Countries' (2009) 34 *International Research Journal of Finance and Economics* 29.

<sup>4</sup> Harrold D Skipper and Robert W Klein, 'Insurance Regulation in the Public Interest: The Path Towards Solvent, Competitive Markets' (1999) Center for Risk Management and Insurance Research, Georgia State University, Paper prepared for The Coordinating Committee on International Insurance Issues Coalition of Service Industries, 11-22

organizations. The country has been described as a ‘truculent African Tragedy’ which has been reduced from the ‘giant of Africa’ to ‘a comatose midget’<sup>5</sup>. This is attributable to lack of a well-coordinated trade policy, poor legal and institutional framework of many sectors of the economy and over dependence on oil and gas sector. Nigerians have thus been thrust into the vicious cycle of poverty<sup>6</sup> as a result of this and other problems relating to political instability and corruption among other problems.

Scholars are however of the opinion that the economic growth and development of Nigeria lies with the diversification from the oil sector and growth of the non-oil sector<sup>7</sup>. This study argues that the Nigerian Insurance Industry (NII) can deliver growth functions to the Nigerian economy within an effective legal and institutional framework. It further argues that the 1972 Indigenisation Decree that led to the exit of foreign insurers is at the root of current state of the NII, hence the need for greater openness not only to strengthen the industry, but to possibly allow for the return of foreign insurance providers.

The thesis therefore posits that liberalising the NII within the WTO/GATS framework will increase the potential of the sector to make positive contributions towards

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<sup>5</sup> George B. N. Ayittey, ‘Nigeria’s Struggle With Corruption’ (A testimony before the Committee on International Relations’ Subcommittee on Africa at the US House of Representatives , Washington DC, Thursday May 19 2006) [http://www.globalsecurity.org/military/library/congress/2006\\_hr/060518\\_3-transcript.pdf](http://www.globalsecurity.org/military/library/congress/2006_hr/060518_3-transcript.pdf) accessed 12 August 2011.

<sup>6</sup> Omololu Fagbadebo, ‘Corruption, Governance and Political Instability in Nigeria’ (2007) 1 African Journal of Political Science and International Relations 028,029.

<sup>7</sup> WTO, ‘Trade Policy Review Report by Secretariat: Nigeria’ (2011) WT/TPR/S/247Executive Summary, para 14 <[http://www.wto.org/english/tratop\\_e/tpr\\_e/tp347\\_e.htm](http://www.wto.org/english/tratop_e/tpr_e/tp347_e.htm) > accessed 31<sup>st</sup> July, 2011; Michael L Ross, ‘Nigerian Oil Sector and the Poor’ (2003) DFID “Nigeria: Drivers For Change Program”, 16 <<http://www.sscnet.ucla.edu/polisci/faculty/ross/NigeriaOil.pdf> > accessed 22nd April 2011

economic growth and development of Nigeria. There is growing interdependence amongst nations of the world which is resulting in the convergence of rules and regulations therefore countries cannot operate in isolation of global trends. This convergence in regulations has led to a growing impetus among nations especially developing countries to fashion their regulatory framework after globally accepted standards. Though this may have some undesirable effect on domestic regulatory autonomy<sup>8</sup>, this thesis argues that there is need for countries to make trade-offs in this regard in order to guarantee better living standards for their citizens. The rules and principles of the WTO/GATS framework offer guidance for domestic reform process<sup>9</sup>. Besides, Nigeria's development strategy in recent years is an outward oriented, export led growth and liberalisation strategies<sup>10</sup>. Therefore, this thesis fits into government's main strategic developmental plans.

This thesis notes criticism of the WTO as lacking 'democratic standards of accountability' because it is believed to be accountable through its internal processes only to some few powerful states and the EU<sup>11</sup>. Also, there are questions on the origin of its rules whether they are designed to benefit all or few<sup>12</sup>. Liberalisation has also been criticised by some economists<sup>13</sup> as an inadequate tool for development but this thesis argues that the key to economic growth and development is not in condemning

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<sup>8</sup> Jan Wouters and Dominic Coppens, 'GATS and Domestic Regulation: Balancing the Right to Regulate and Trade Liberalisation' in Kern Alexander and Mads Andenas (eds) *The World Trade Organisation and Trade in Services* (Martinus Nijhoff, 2008) 209.

<sup>9</sup> UNCTAD, Ad Hoc Expert Meeting on Insurance Services (Geneva, 24 November 2005) para 30.

<sup>10</sup> Dani Rodrik identifies three which are Import Substitution, Outward oriented and the Two Track strategy

<sup>11</sup> Robert O Keohane, 'Global Governance and Democratic Accountability' Chapter prepared for a volume to be edited by David Held and Mathias Koenig-Archibugi from the Miliband Lectures, London School of Economics, Spring 2002, 18-19.

<sup>12</sup> Dani Rodrik, *The Globalization Paradox: Democracy and the Future of the World Economy* (Norton 2011)83.

<sup>13</sup> Dani Rodrik, Robert O. Keohane and Joseph S. Nye and Joseph E. Stiglitz.

global economic integrations or convergence but in strengthening policies that ensure its success. Globalisation has been acknowledged to be a ‘positive force’ when ‘domesticated’ in a way that works for the country and not against it like it was done in Asian countries<sup>14</sup>. The option of protectionism will portend very negative circumstances for all nations of the world especially people in developing countries like Nigeria. This thesis proposes reforms using WTO/GATS rules and principles as a model or standard but does not suggest a fixed set of rules. Rather, the application of globally accepted regulatory principles to the peculiarities of the Nigerian financial sector for the effectiveness of the legal and institutional reforms in the NII.

This study also argues that liberalisation is also necessary for the development of the NII first because of the mutual independence between financial services development and economic growth<sup>15</sup>, and secondly because of the nature of insurance services.

Studies have revealed that a weak financial system lacking capital is a solid barrier against development. On the other hand, insurance is an infrastructural financial service the liberalisation and development of which would positively affect the overall economy of the nation by increasing productivity entirely. Insurance supports entrepreneurial activities and increases income and wealth. Insurance policies provide growth and socio-economic functions<sup>16</sup> which positively affect the welfare of people and alleviate the poverty challenges in the economy. These developmental functions of insurance however vary among different categories of insurances. While Personal

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<sup>14</sup> Rodrik (n12) 146.

<sup>15</sup> UNCTAD, ‘Trade in Services and Development Implications’ (2003) UNCTAD TD/B/COM.1/62; para 10 <[http://www.unctad.org/en/docs/c1em33d3\\_en.pdf](http://www.unctad.org/en/docs/c1em33d3_en.pdf)> accessed 23<sup>rd</sup> April 2011

<sup>16</sup> See discussion in chapter two.

insurances<sup>17</sup> provide more direct social welfare functions, commercial insurance<sup>18</sup> policies on the other hand facilitate trade and economic growth. Nonetheless, both categories of insurance policies have positive implications for the economy such as increasing GDP which translates into improved welfare and lower poverty levels in the country. Therefore, the liberalisation of insurance is necessary in all classes of insurance because the goal of insurance sector liberalisation and development is the increase in welfare and reduction of poverty within the economy.

The GATS model for reforms provide flexible regulatory parameters upon which developing countries can hinge their domestic reforms progressively and gradually without such pressures witnessed under the bilateral or preferential trade agreements or developmental institutions. The WTO/GATS model is a rules and principles platform for the liberalisation of insurance services incorporating rule of law in international economic transactions. These principles provide a model which would help create enabling regulatory structures in the NII that would assist in resolving market failures, and pursue socio-economic goals with economic efficiency. As a rule based platform, it highlights the importance of rule of law in trade and development. It therefore presents rules and the decisions of various panels as a guide for regulatory reforms because legislations would be enacted with full knowledge of their implication for both domestic and international service suppliers.

Therefore, rather than view the GATS as an ‘hegemonic construct’ or as a form of ‘legal imperialism’ designed to further the goals of industrialised countries to ‘rewrite

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<sup>17</sup> Such as fire, motor, burglary, life etc.; see also analysis of classes of insurance in s2.1.

<sup>18</sup> Such as Marine, Aviation, Oil and Gas

the rules of domestic regulation of services'<sup>19</sup>, this thesis focuses on the use of GATS as both a legal and ideological model for service sector regulatory reforms. It places not much emphasis on the origins of the GATS and its rules, but rather on the use of its legal ideology for the advancement of the objective of economic development in Nigeria.

This research also notes the criticisms against the use of economic growth as a perspective for development such as Sen's<sup>20</sup> suggestion that development should be considered from a wider perspective of real freedoms and not from the perspective of economic growth alone. This thesis however argues in chapter two that economic growth needs to take pre-eminence in developmental programmes because without the former the latter may amount to a 'wild goose chase'.

Law and its enforcement matters in the development of financial markets and this thesis argues that the NII needs to be unilaterally liberalised through effective legal and institutional reforms which emphasises the rule of law and adopt a competition policy that allows new entrants whether domestic or foreign<sup>21</sup>. There is need for the infusion of competition facilitated by adequate, impartial, minimally intrusive and transparent regulations which will strengthen the domestic landscape for better

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<sup>19</sup> Jane Kelsey, *Serving Whose Interest: The Political Economy of Trade in Services Agreement* (Routledge-Cavendish, 2008) 24, 58.

<sup>20</sup> Amartya Sen, *Development as Freedom* (Knopf Inc, 1999)

<sup>21</sup> John C. Coffee, 'Law and the Market: The Impact of Enforcement' (2007), Centre of Law and Economic Studies WP 304 < <http://www.cbe.anu.edu.au/capitalmarkets/papers/COFFEE-CAPITAL-MARKETS.pdf> > accessed 15th August 2011; La Porta et al, 'Legal Determinants of External Finance' (1997) 52 *Journal of Finance* 1131; La Porta et al, 'Law and Finance' (1996), 105 *Journal of Political Economy* 1113, it is important to note that though the studies of La Porta et al were novel and reference points in most legal research on financial markets, most of the indices used in their work has since been queried such as in H. Spaman, 'Law and Finance Revisited' (2008) Havard Law School John M Olin Centre Discussion Paper 12 < [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=1095526](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1095526) > Downloaded 15<sup>th</sup> August 2011. It is also pertinent to note that most of these studies were concentrated on stock markets.

efficiency for the NII to be able to deliver growth to the GDP of Nigeria. The principles and rules of the WTO/GATS offer regulatory models on which the reforms in the domestic turf can hinged for efficiency, improved performance and greater openness prior to further commitments by the Nigerian government in the GATS. As postulated by Ringer<sup>22</sup>, all reforms need to ‘establish clear institutional benchmarks’ to measure its success or failure. This would make Nigeria’s future attempt at deeper commitment in the GATS easier.

The option of regional integration like AU, ECOWAS or bilateral agreements such as the New Partnership for African Development (NEPAD) were considered but not preferred. On the regional level, Nigeria is surrounded by poor struggling LDCs and the African and West African regional integration efforts have been faced with a myriad of problems. These constraints are related to size, unfavourable economic contexts and divisive colonial alliances of African countries mainly. Unlike other regional economic unions, there has been low commitment towards achieving the goals of trade agreements and important milestones for the implementation of the provisions of the Agreements have never been met<sup>23</sup>. ECOWAS lacks the commitment, financial and human resources to pursue its proposed customs union and unified monetary largely because of subsisting colonial alliances. In the same vein, PTAs and other development programmes in Africa have also suffered from the introduction of non-trade related intrusive clauses as preconditions in trade agreements.

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<sup>22</sup> Thom Ringer, ‘Development, Reform, and the Rule of Law: Some Prescriptions for a Common Understanding of the “Rule of Law” and its Place in Development Theory and Practice’ (2007) 10 Yale Human Rights and Development Law Journal, 182.

<sup>23</sup> Olumuyiwa Alaba, ‘EU-ECOWAS EPA: Regional Integration, Trade Facilitation and Development in West Africa’ Paper delivered at GTAP Conference, UNECA (Addis Ababa, May, 2006) 7.

The multilateral framework of WTO/GATS is therefore preferred as a viable model for the successful liberalisation and development of the insurance sector<sup>24</sup> because it is a rule and principles based regime allowing for a greater level of regulatory and political autonomy of countries leaving out non-economic issues in the negotiations for trade. It is a platform that affords flexibility, credibility and technical support which LDCs liberalisation programmes would benefit from.

This thesis however follows the ‘free trade’<sup>25</sup> school of thoughts of Hudec<sup>26</sup>, Trubek and Cottrell<sup>27</sup>, and more recently Thomas and Trachtman<sup>28</sup> which posit that reliance on Special and Differential Treatment (SDT)<sup>29</sup> under international trade arrangements would not deliver economic prosperity and development to Less Developed Countries. Hudec had argued that it would harm these countries than help them because it encourages the protection of inefficient industries ‘under the assumption that infant developing countries can be helped by infant industry policies’<sup>30</sup>. He further argues that politicians in these countries would be encouraged to use import protection as solution to economic problems<sup>31</sup>. On the other hand, incorporation of international of trade norms facilitates greater openness and growth in developing countries. This thesis therefore puts up a case for liberalisation of the NII using the

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<sup>24</sup> It has been successful in other LDCs like China and India.

<sup>25</sup> This is a term coined to mean scholars that believe that free trade rather than SDTs was the sure path for economic growth and development of developing countries.

<sup>26</sup> Robert Hudec, *Developing Countries in the GATT Legal System* (Gower, 1987) 159-160

<sup>27</sup> David Trubek and M. Patrick Cottrell (n49) , Robert Hudec and the Theory of International Economic Law: The Law of Global Space’ (Inaugural Conference of the Society of International Economic Law, Geneva Switzerland, July 2008) 30.

<sup>28</sup> Chantal Thomas and Joel P Tractman , *Developing Countries in the WTO Legal System* (OUP, 2009)21-22

<sup>29</sup> *ibid* 23; SDTs originated from the GATT 1979 Enabling Clause and this has been included in all WTO Agreements.

<sup>30</sup> Hudec (n26)159-60.

<sup>31</sup> *ibid* 170.

WTO/GATS model, preparatory to further negotiations and locked in commitments in the framework.

This study submits that liberalisation of the NII with regulatory principles of the WTO/GATS should be juxtaposed with regional trade efforts to afford the neighbouring countries the opportunity to leverage the gains of trade from Nigeria. It would also facilitate the country's emergence as a regional economic giant which ought to be.

## **RESEARCH METHODOLOGY**

This thesis is a reformist research in financial market that presumes that law shapes and facilitates market transactions by providing the 'essential framework for them to occur'<sup>32</sup>. The thesis argues that enacting the right rules and properly enforcing them would solve market problems.

The study applies a multi-method approach<sup>33</sup> because a dearth of research exists in the area of insurance regulation and no systematic collection of empirical data could be found on which theory could be built<sup>34</sup>. It therefore uses more than one research technique to provide a more 'nuanced understanding of law, legal institutions, and legal processes' in the NII. The traditional legal method of research i.e. doctrinal technique is combined with social science survey research techniques<sup>35</sup> to enrich the

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<sup>32</sup> Julia Black, 'Financial Markets' in Peter Cane and Herbert M Kritzer (eds) *The Oxford Handbook of Empirical Legal Research* (OUP 2010) 151-175.

<sup>33</sup> Laura Beth Nielsen, 'The Need For Multi-Method Approaches in Empirical Legal Research' in Peter Cane and Herbert M Kritzer (eds) *The Oxford Handbook of Empirical Legal Research* (OUP 2010) 953-956.

<sup>34</sup> Most of the research in financial markets have been centred around capital markets and banks e.g La Porta et al (n21), Coffee (n21) and so on.

<sup>35</sup> Often referred to as Socio-Legal Techniques of research in Legal Research

quality of this research.

### Research Hypothesis

In the light of the problem forming the research background, the study derives the hypothesis that:

**“The regulatory principles of the General Agreement on Trade in Services (GATS) under the World Trade Organization (WTO) is a viable model for promoting the liberalisation of the NII”**

### Research Questions

In solving the problem of the NII, some questions which this research addresses in detail through relevant chapters of this thesis include:

- i. Are there trade restrictions in the legislative and supervisory framework of the NII?
- ii. To what extent does legislative and supervisory framework of the NII's deviate from the liberalising model of the GATS?
- iii. To what extent does the legislative and supervisory framework affect the NII's liberalisation in GATS?

This thesis makes a modest contribution to the relatively small but growing field of research into the insurance law and practice in Nigeria<sup>36</sup> and it uses the Nigerian circumstance as an example for further developmental studies on LDCs globally.

### Research Design

This is a qualitative cross-disciplinary study<sup>37</sup> which uses a multi- method research technique to investigate the structure, form, processes and legal environment of the

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<sup>36</sup> J.O Irukwu, Insurance Law and Practice In Nigeria (Heinman 1971);

<sup>37</sup> It cuts across law and social sciences by proffering legal solutions to economic problems.

NII in order to identify the factors affecting the liberalisation of the sector<sup>38</sup>. It therefore employed both legal and non-legal methods of research i.e. doctrinal and non-doctrinal research techniques<sup>39</sup>.

The legal methods of research are doctrinal and critical analysis of the regulations affecting the NII and the WTO/GATS agreements. The critical analysis of the WTO/GATS framework reveals its liberalisation model for insurance while detailing some of its shortcomings. Furthermore, NII regulations were also critically assessed on the basis of the constructed parameters from this model in chapter four. The analysis revealed the trade restrictive aspects of the NII legislative and institutional framework and identified areas for possible reforms.

Primary legal sources such as legislation and international agreements and secondary legal sources such as, books, journals, working papers, conference papers and electronic sources are also consulted. The secondary sources were employed as tools of critical analysis of the primary sources of laws. The research also made effective use of finding tools<sup>40</sup> like bibliographies and most importantly, people and organizations which helped provide information about critical areas of the study

This study also included a socio-legal exploratory survey conducted on a cross section of stakeholders in the NII. The aim was to use data from that exercise to understand the regulatory environment of the NII and to possibly complement the legal analysis.

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<sup>38</sup> David R Maines, 'Social Organization and Social Structure in Symbolic Interactionist thought' (1977) 3 Annual Review of Sociology 235, 256.

<sup>39</sup> Ian Dobinson and Frances John, 'Qualitative Legal Research' in Mike McConville and Wing Hong Chui (eds) *Research Methods of Law* (Edinburgh UP 2010) 18-9.

<sup>40</sup> Hoofman Rumsey, *International and Foreign Legal Research: A Coursebook* (Martinus Nijhoff (2007) 14-5.

The survey involved the designing of a research instrument and a sampling technique; a structured questionnaire, delineating of population of interest, selecting methods of data collection, analysis and presentation of findings.

Data used in the survey were from two sources i.e. primary and secondary sources of data<sup>41</sup>. Primary data was generated through survey conducted while the secondary data is from all other legal<sup>42</sup> and non-legal sources. The primary data from the survey were statistically analysed and the findings presented in chapter six.

### **Survey Research Population and Sample**

The research population was the entire stakeholders in the NII which include all insurance companies, insurance brokers, insurance regulators, shareholders and insurance policyholders<sup>43</sup>. This population was large therefore a sample was drawn to ‘generalise from the properties of the sample to the broader population’<sup>44</sup>.

The choice of sampling method is dependent on the availability or otherwise of a sampling frame<sup>45</sup>. Random sampling methods require a sampling frame which was not available for this study for all elements of the survey<sup>46</sup>. Therefore a non-random purposive snowball sampling<sup>47</sup> which uses expert judgment in selection of a sample

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<sup>41</sup> Wing Hong Chui, ‘Quantitative Legal Research’ in Research’ in Mike McConville and Wing Hong Chui (eds) *Research Methods of Law* (Edinburgh U P 2010) 57.

<sup>42</sup> Primary and Secondary sources of law are both secondary data sources.

<sup>43</sup> Patrick Sturgis, ‘Designing Samples’ in Nigel G Gilbert (ed) *Researching Social Life* (3<sup>rd</sup> edn, SAGE 2008) 167.

<sup>44</sup> *ibid.*

<sup>45</sup> A sampling frame is a list containing all the elements of your research population.

<sup>46</sup> none for all insurance policyholders in Nigeria.

<sup>47</sup> This is also referred to as non-probability sampling ; Charles Teddlie and Fen Yu, ‘Mixed Methods Sampling : A Typology With Examples’ (2007) 1 *Journal of Mixed Methods Research* 77, 80.

size of 30 or less and focuses on generating in depth narrative data was employed.<sup>48</sup> It is ‘based on social network logic whereby people are linked by a set of social relationships and contacts. Respondents are asked to name possible respondents ‘based on an inclusion criteria defined by the researcher’<sup>49</sup>. The survey gained ‘in-depth and intimate information’<sup>50</sup> from a sample size of 10. The initial four (4) respondents were chosen based on their knowledge of insurance law and administration in Nigeria. This included two insurance chief executives, one NAICOM official and one insurance broker. The two insurance executives named three other executives while the insurance broker selected another insurance broker and two well informed policy holders to make the sample size of 10. On the whole the sample included five (5) insurance executives, two (2) insurance brokers, two (2) policyholders and one (1) senior executive from NAICOM.

The sample had a higher number of insurance executives because they are the focal point of insurance supervision world over and the bulk of NAICOM’s activities revolve around them. Besides, insurance executives are a politically active interest group usually in debates regarding trade in insurance services<sup>51</sup>. In Nigeria, due to constant interaction with supervisory officers, they have greater understanding and knowledge of NAICOM’s operations more than other stakeholders in NII.

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<sup>48</sup> *ibid* 84; examples are Quota and Snowball Sampling.

<sup>49</sup> Rebecca D Petersen and Avelardo Valdez, ‘Using Snowball-Based Methods in Hidden Populations to generate a Randomized Community Sample of Gang-Affiliated Adolescents’ (2005) 3 *Youth Violence and Juvenile Justice* 151, 154.

<sup>50</sup> Anne-Marie Ambert et al, ‘Source Understanding and Evaluating Qualitative Research Author(s)’ (1995) 57 *Journal of Marriage and Family* 879, 880.

<sup>51</sup> Insurance executives greatly influences the trade policies of their government with regards to their sector as evidenced in US and UK insurers lobbying during the process of China’s liberalisation of its insurance sector; Stephen P. D’Arcy and Hui Xia, ‘Insurance and China’s Entry into WTO’ (2003) 6 *Risk Management and Insurance Review* 7, 18.

This study argues that the size of the sample is sufficient due to the exploratory nature of the survey research which requires small samples and need not be representative. The research in this study to provided awareness and understanding on the NII regulation and administration due to the non-existent theory and legal research in this area. It therefore seeks to generate insights<sup>52</sup> into this new area of research which included information on the regulatory policies and practices which would not have been evident from the analysis of the legal framework of the NII. The findings from doctrinal analysis and the survey research are therefore mutually complementing and form part of one whole research rather than two different types of research. Nonetheless, the data and instrument for data collection are valid and reliable. Instrument discussed below asked questions relevant to the research and provided reliable data though the sample may not be representative and therefore limiting the extent of its generalization. It is further argued that the objectives of the survey research were fulfilled because of the greater insights on the administration of the NII gathered.

### **Research Instrument**

This was a structured questionnaire divided into three (3) sections A, B and C and containing questions on all the parameters identified in the analysis of the WTO/GATS model of liberalisation of insurance. It contained open ended questions which had the advantage of ‘allowing interviewees develop answers much more fully’<sup>53</sup> rather than limited and clear ones expected of closed questions.

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<sup>52</sup> Martyn Denscombe, *Ground Rules for Social Research: Guidelines for Good Practice* (Open University Press 2009) 11, 105.

<sup>53</sup> Sturgis (n43) 193

Section ‘A’ questions related to IAIS core principles for effective insurance supervision and focuses on NAICOM mainly. It was divided into seven (7) subsections as arranged in the IAIS document<sup>54</sup>. The first subsection was on conditions for effective insurance while the second was on the supervisory system. Subsection 3 dealt with questions relating to NAICOM’s activities with supervised entities i.e. insurance companies, and insurance intermediaries and Subsection 4 had questions on on-going supervision of NAICOM such as market analysis, off-site and on-site monitoring. Subsection 5 inquired on the extent to which NAICOM met the prudential requirements of a supervisory body while subsection 6 questions were on the activities of NAICOM with regards to the control the insurance market and consumer protection. The final section dealt with questions relating to anti-money laundering and financing terrorism activities of NAICOM.

Regulatory principles and compliance with the WTO Insurance Model are the focus of Sections B and C of the questionnaire respectively. Respondents were asked to identify the regulatory principles used in Nigeria. The last part of the questionnaire contained questions relating to Nigeria’s level of compliance to the Insurance Model in various modes of market access and with the Best Practice section of the Model.

### **Data Collection**

Data was collected through structured interviews asking respondents questions from the questionnaire in the pre-determined order and recording responses. The respondents were approached, promised confidentiality and anonymity of their responses and thereafter asked to sign an Informed Consent Form before the

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<sup>54</sup> These principles are discussed in s4.2.3.

commencement of the interviews. The interviews were conducted in the offices of respondents or anywhere requested by them. Explanations of questions were offered and responses were typed directly into a laptop. The transcription was not verbatim but relevant notes on the question asked and issues of importance to the research were typed in as responses.

It is pertinent to note that an ambitious sample size of 25 was initially planned but the poor response in the field as a result of respondents lack of interest in research work coupled with busy schedules of executives accounted for small sample size. Nonetheless, it took nine months to get all the 10 respondents fully interviewed.

The interviews were in two batches with the first involving the initial four respondents selected by the researcher and it took place between March and June 2010 while the second set of respondents were interviewed between June and November 2010. Most respondents required at least two sessions to complete the structured interview.

### **Method of Data Analysis**

Responses from the interviews were analysed using tables and percentages. Tables were constructed with columns to show agreement, disagreement and other opinions such as lack of knowledge or extra comments of respondents. The use of more sophisticated statistical analysis was considered not necessary because of the small number of respondents involved in exercise.

### **Justification of Research**

A great deal of poverty and suffering is experienced in many LDCs therefore

economic development and growth is highly desired to improve living standards in and alleviate sufferings in these poor nations. Developmental studies continue to research ways of achieving this goal and this study makes unique contributions by its using the novel approach of insurance liberalisation and the NII. Insurance though not often considered as a developmental tool is highlighted as a viable key to unlock the growth potential of developing countries.

The choice of Nigeria is informed first by its position in Africa as an active player and the world generally. Secondly, Nigeria possesses a lot of influence in her region such that should the problem of economic growth be solved in Nigeria, it would rub off positively on the neighbouring countries in the sub-region and Africa as a whole.

Furthermore, being the most populous country in Sub Sahara Africa (SSA) with a population of over 150million its large population represent opportunities and potentials on which trade can be hinged.

Nigeria also stands to benefit under multilateral arrangements with influx of much needed capital for growth and development of the economy. The introduction of innovative market systems alongside the liberalisation of insurance in Nigeria would well position Nigeria as a regional economic power rather than the sleeping giant it now symbolizes.

Furthermore, Nigeria is an active and respected member of the WTO. An increase in its commitment levels in the GATS would spur other developing countries into embracing the growth opportunities available under the framework other than

clamouring for more preferential treatment which has not achieved any developmental goal.

Finally, the credibility of the liberalisation effort of a sector determines the extent of its success. The global acceptance success of the WTO/GATS framework informs its choice as liberalisation model for the NII.

### **Limitations of the methodology**

All the methods of research used present limitations on the study. For the doctrinal approach, there is the danger of a highly descriptive analysis. Consequently, this study devised a critical approach to the analysis of the legal texts. Furthermore, the author being mindful of the need for objectivity of the analysis presented was careful with the use of secondary source of law. Corroboration of information from various sources was the strategy used to ensure objectivity of the research data.

The socio-legal techniques involving sampling technique, sample size and method of data analysis also had its limitations. The use of a non-random sampling technique may have introduced some bias in the selection of respondents which may have affected the findings from the survey. Furthermore, a sample size of ten (10) limits the extent to which generalizations could be made on the results derived because of the issue of representativeness of the sample. The use of percentages and tabulations may also have deprived the study of more accurate statistical findings.

Nonetheless, the socio-legal technique did serve the purpose for which it was used mainly by enriching the data upon which this study based its findings, conclusions

and recommendations. The research is chronicled in this thesis in eight chapters as shown below.

### **Outline of the Thesis**

This thesis is divided into eight (8) chapters with each chapter consistently addressing aspects of the main themes of this research which are first, that insurance has growth potentials and secondly that well regulated and liberalised insurance sector under the WTO/GATS model can deliver it. Therefore, the NII needs to be reformed in line with this model of reforms for insurance liberalisation.

Chapter one provides the contextual framework of the thesis by analysing post-independence developmental challenges in the Nigerian economy generally and the structural and regulatory challenges of the NII. It makes a case for the development of the non-oil sector and justifies the use of liberalisation as the key to ensuring greater openness and growth for the Nigerian economy in general and the NII in particular by unlocking the growth potentials of the sector.

The chapter traces the root of developmental problems in Nigeria to the abandonment of the non-oil sector since the oil boom period of 1970s. It reveals that the GDP depends heavily on oil income which is susceptible to fluctuations and gets the country 'stuck in the periphery of the world economy'. It notes further that reforms in the last decade in the country had yielded not much result in terms of improving the socio-economic wellbeing of citizens. It canvasses for the NII as a non-oil sector with potentials for economic growth.

The structural challenges of the NII were identified to include low capacity,

inadequate legal and supervisory framework, poor human resource and market practices. These together with poor insurance culture and awareness account for low insurance penetration and density in the NII. The chapter argues that greater reforms and liberalisation would be required to promote market efficiency and competition to facilitate the NII's delivery of growth to the economy with due consideration of recent literature on liberalisation.

Chapter one concludes with an analysis of Nigeria's participation in regional and multilateral trade relations highlighting the problems with regional trade. It canvasses for more liberalisation and locked in commitments within GATS to support reform programmes to ensure that the developmental goals of Nigeria is achieved through increasing economic growth.

Chapter two examines insurance services from its functional and regulatory perspective and aligns with the economic growth theory on development. The analysis reveals the traditional functions which included social services, financial stability of individuals and businesses, provision of investment funds, management of risk portfolios of the nation among others. It also examines its potential for growth as recorded in empirical work of scholars though noting criticisms against the economic growth perspective on development such as Sen's. The chapter argues in support of the liberalisation of the insurance sector while reiterating adequate regulatory measures to facilitate its effectiveness. It therefore presents insurance regulatory instruments and strategies together with benefits and challenges therein.

Chapter three is divided into two parts with the first offering an analysis of

liberalisation in theory and within the context of the WTO/GATS while re-emphasising the need for proper regulations for its effectiveness. The examination of the principles of WTO reveals the positive prospects of using the model as a liberalisation framework. The study argues that more liberalisation enhances the potential and success for global trade participation as opposed to Special and Differential Treatments (SDTs) which have no guarantees attached within the framework. It concludes that a well supervised insurance sector accompanied with effective liberalisation would facilitate the growth potentials of the sector.

The second part of chapter three examines GATS as a legal text, a service trade ideology and a model for regulatory reforms. It therefore discusses the structure of GATS, which include its definition of service and its four modes of trade. The chapter also highlights the GATS regulatory model for liberalisation and reforms which emphasises flexibility and progressiveness but also include a distinction between general and specific obligations, domestic regulatory principles, economic integration and technical cooperation with LDCs amongst others.

Chapter Four specifically focuses on GATS liberalisation framework for insurance services starting with the GATS Annex on Financial Services and its pertinent provisions such as the prudential carve out. The contributions of other models such as the Understanding on Financial Commitments and the regulatory model of the Insurance Model schedule and Best Practices deriving from the GATS model were also examined. Similarly, the global standards of insurance supervision provided by the International Association of Insurance Supervisors (IAIS) principles were also analysed. It also examined market access and current negotiations in insurance in the

GATS.

This chapter establishes the fact that the GATS framework provides both comprehensive parameters and effective platform for the liberalisation of the NII for economic growth in Nigeria. It therefore concludes with a construction of legislative and institutional parameters for effective liberalisation of insurance sectors based on the analysis in this chapter and the preceding three chapters. This formed the bases of the GATS model of reforms used in the analysis in chapters five and six. The legislative parameters embrace principle-based regulations, risk based regimes and removal of restrictions on market participation. Institutional parameters require having an independent supervisory agency with clear objectives, adequate authority, sufficient power, resources, and transparency which cooperates with other regulators.

The legislative aspects of the GATS model of reforms is the basis of analysis in chapter five where it is benchmarked against the legal framework of the NII. The analysis begins by clearly outlining the model and stating the legislations which form the legal environment of the NII. This is followed by a critical analysis of these laws in three parts. The first addresses elements of the law that do not conform to Nigeria's obligations in the GATS and the model of reforms and therefore needs to be changed. The second part of the analysis examines elements of the law which complies with Nigeria's obligations but not sufficiently liberal. The final part details elements of the law that complies with Nigeria's multilateral obligations and model of reforms for liberalisation.

The chapter concluded with the observation that the commercial mode of trade was

more favoured in the NII legal framework though a fragmented set of requirements and conditions exist in legislations which foreign insurers need to fulfil to establish commercial presence. These include mandatory incorporation, insistence on a particular type of insurance organisations and the interference in the internal administration of foreign firms. The analysis further reveals the non-application of risk based or principle based regulations and reforms were therefore suggested in the above areas including the improvement of market participation in other modes of trade for greater liberalisation.

Chapter six continues the legal analysis by focussing on the institutional framework and implementation of insurance laws in NII. The chapter examines the NAICOM Act against the institutional model of reforms. The analysis reveals that the Act provides clear objectives, but without adequate powers, funding, and staffing for the Commission. Independence, transparency and accountability of the Commission is also not guaranteed under the Act. Furthermore, the surveillance mechanism was also inadequate in terms of frequency and breath. The chapter argues for a Bi-Polar system of financial regulation for the purpose regulatory resource sharing and cooperation among non-bank regulators in the financial sector to meet the resource and staffing inadequacies. The option of building capacities through partial market opening and allowing the regulator 'learn by doing' is examined but due to ineffective surveillance and impact assessment mechanisms the study opined that that form of experimentation would not succeed as it had in the EU. Rather, the thesis argues that institutional reforms aimed at capacity building would be more effective in the NII presently.

Chapter seven presents data from the survey research conducted on the NII. The responses confirm the conclusions from the doctrinal analysis and made some other revelations. These include NAICOM's compliance with IAIS standards of licensing and corporate governance enforcement. These findings complemented the analysis in the earlier chapters of the thesis. The chapter further confirms the inadequacy of the NAICOM Act with regards to supervising a liberalised NII. The findings were however contradictory on transparency which was attributable to differing standards of transparency being expected when the regulator is dealing with the regulated and the public. The standards expected when dealing with the regulated was higher than with the public.

Nonetheless, the chapter argues for further liberalisation through the model of institutional reforms being suggested by the study which are the adoption of regulatory principles especially transparency, proportionality, independence and accountability coupled with risk based regulations and supervision.

Chapter eight presents all the findings from all earlier chapter and conclusions drawn from them.

In conclusion, this introduction summarises the entire thesis, the methodology and justification for the research. The next chapter presents the background of the study, highlighting the problems with the NII and arguing for the liberalisation of the sector to enhance the potentials for economic growth in Nigeria.

## CHAPTER ONE

### NII AND THE NEED FOR LIBERALISATION

#### 1 INTRODUCTION

Nigeria is the largest country in South Sahara Africa (SSA) located on the west coast and at the eastern terminus of the bulge of West Africa. It has a boundary of about 924,000 square kilometres<sup>1</sup> that cuts across many cultural and physical boundaries resulting from its colonial history. Nigeria is the most populous country in Africa with a population of about 154million, almost half of the population of West Africa. It is made up of over 200 ethnic groups and its geographical, ethnic and cultural identity is fragmented but arranged along six geopolitical zones.

Nigeria attained independence in 1960 from Britain when power was handed over to an elected government. The country had been under military rule for years but the last eleven (13) has been under a fragile but stable democracy. Nigeria's federal republic<sup>2</sup> is modelled after the United States of America with executive powers exercised by the president and checked by the National Assembly consisting of the Senate and the House of Assembly<sup>3</sup>. The fourth democratically elected government was sworn in May 2011 after a transparent and credible election.

This chapter presents a contextual background to the insurance system in Nigeria. It

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<sup>1</sup> Fidel Ezeala- Harrison, 'Structural Re-Adjustment in Nigeria: Diagnosis of a Severe Dutch Syndrome' (1993) 52 AJES 2,194

<sup>2</sup> Other systems of government had been practiced in the past.

<sup>3</sup> The Bi-cameral nature of the House of Assembly resembles the system in West Minster. Britain.

gives a brief geographical context, presents a historical analysis of the development of insurance regulation in Nigeria and the Nigerian legal system. Given the correlation between insurance system and the economy, this chapter also presents the economic outlook. The chapter aims to make a case for liberalisation of insurance sector as the vital key for growth and development of the Nigerian economy.

## **1.1 NIGERIAN LEGAL SYSTEM**

The sources of law in Nigeria are the Nigerian Constitution, Nigerian legislation, and English law, Customary Law, Islamic Law and Judicial Precedents. The constitution is supreme in the hierarchy of laws and all other laws take authority from it. Nigerian legislations consist of the statutes, ordinances, Acts, Laws, Decrees and Edicts.

The English Laws applicable in Nigeria are the Received English laws<sup>4</sup> and other English laws enacted and extended to Nigeria before its independence which is yet to be repealed. Customary law evolved from traditional norms and practices of the different ethnic groups mainly in the southern part of Nigeria. Sharia law is the Islamic law used since pre-colonial times in the northern part of Nigeria where the population is predominantly Muslim. Therefore four distinct systems of law exist in Nigeria originating from its colonial past and its rich cultural heritage. The English Law and Common Law from Britain, the customary law and the Sharia derived from pre-colonial times that have been adapted into the Nigerian legal system law. In the hierarchy of courts the Supreme Court is the apex while Customary, Sharia and Area courts form the base of the judicial branch.

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<sup>4</sup> This consists of the common law, equity, statutes of general application and statutes and subsidiary legislation on specified matters.

Regulations affecting the NII have been enacted by the federal legislators who derive their powers under various constitutions since independence. Currently, S.4 (1) of the 1999 Constitution of The Federal Republic of Nigeria vests the powers to legislate matters on the Exclusive List (of which insurance is Item No. 33) on the National Assembly consisting of the Senate and the House of Assembly. The liberalisation of the NII would therefore require an enactment of a new IA or amendment of IA of 2003 to reflect a commitment to the liberalisation of the sector.

## **1.2 HISTORICAL PERSPECTIVES OF INSURANCE REGULATIONS IN NIGERIA**

The modern form of insurance was brought into Nigeria by the British<sup>5</sup> (with the intention of servicing the needs<sup>6</sup> of the British trading activities along the West Coast of Africa) therefore, the practice of insurance in Nigeria was and is still patterned after that of Britain. The regulation of NII also dates back to colonial times when insurance regulations in Britain were applicable in Nigeria. This period had mainly foreign based insurance companies<sup>7</sup> ‘registered and headquartered’ in United Kingdom (UK)<sup>8</sup>. There was also ‘a near absence’<sup>9</sup> of regulation or control over insurance companies. Companies simply needed to place a statement in their registered and branch offices at inception of business and twice every year<sup>10</sup>.

Laws applicable in colonial times in the NII were Life Assurance Act of 1774, Fire

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<sup>5</sup> In Nigeria traditional forms of insurance were in existence before the colonialist brought in insurance. R.O. Ayorinde, ‘The Pension Reform Act of 2004 and Public Sector Schemes in Nigeria’ (2005) 23JIR4 69, 69.

<sup>6</sup> C U Uche, ‘The regulation of insurance investments in Nigeria’ (1998) 6INTILR 327,

<sup>7</sup> As at independence, of the 25 insurance companies in existence only 4 were indigenous

<sup>8</sup> Ezeala- Harrison (n1) 193-208.

<sup>9</sup> *ibid.*

<sup>10</sup> Companies Act of 1922

Prevention (Metropolis) Act of 1774, Married Women Property Act of 1882, Marine Insurance Act of 1906 and the Gaming Act of 1845. The local law enacted during this period was the Motor Vehicle (Third Party Insurance) Act of 1945.

At independence though Nigeria was a ‘primary product exporting economy with a viable industrial potential’<sup>11</sup>, it was a service importing country. There were large outflows of insurance premiums in reinsurance and investment funds abroad<sup>12</sup> (mainly UK). This drain on the foreign reserves of the country led to the enactment of laws mainly to correct this and other emerging problems.

Post-independence NII legislations also addressed the alarming rise in unscrupulous practices by financially weak companies characterised by poor quality personnel and high insolvencies. The laws therefore addressed issues of minimum share capital and the general need to protect insurance consumers. The investment of insurance funds<sup>13</sup>, mandatory incorporation of all foreign insurance companies and subjecting them to Nigerian taxation laws<sup>14</sup> were also features of post-independence NII regulations to ensure the integrity of the sector. There also existed protectionist laws such as the compulsory insurance of all imports with Nigerian registered companies<sup>15</sup> and the right to 20% compulsory cessions and right of first refusal given to Nigeria Re<sup>16</sup>.

The return to democratic governance in 1999 saw the enactment of the Insurance Act

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<sup>11</sup> Ezeala-Harrison (n1) 197.

<sup>12</sup> Uche (n6) 332a

<sup>13</sup> Insurance (Miscellaneous Provision) Act of 1964.

<sup>14</sup> Insurance Decree of 1968.

<sup>15</sup> Insurance Decree of 1976 but this provision is incorporated into the s67 of IA of 2003.

<sup>16</sup> Insurance Decree of 1977.

(IA) of 2003 and the Pensions Act (PA) of 2004<sup>17</sup> which together with the National Insurance Commission (NAICOM) directives and guidelines form the substantive laws on insurance in Nigeria.

Other laws affecting the NII include Companies and Allied Matters Act of 2004; Nigerian Investment Promotion Commission Act of 2004; Immigration Act of Cap 171 of 1990; Securities and Exchange Commission Acts of 1988,1999 and 2007; and the Foreign Exchange (Monitoring and Miscellaneous Provisions) Act of 2004<sup>18</sup>.

From post-colonial regulatory measures, one can decipher that the fundamental objective of the Nigerian government has always been the promotion of a healthy NII which will make positive contributions to the economy while providing adequate welfare and social services for its citizens. Hence the continuous process of eliminating inefficient and non-performing insurance companies through increasing minimum capital requirement. However, the indigenisation policy of 1972 worked contrary to this objective and the realisation of this fact after over two decades led to the wave of privatisation and reforms witnessed since 1999 which as would be analysed in the next section failed to bring about necessary growth in the NII.

### **1.3 ECONOMIC OUTLOOK AND DEVELOPMENTAL CHALLENGES**

Nigeria is a developing country endowed with both solid and liquid mineral deposits which include petroleum, natural gas, bitumen, tin, iron, ore, coal, limestone and lead. At independence, Nigeria ‘had a strong agricultural sector that was able to support domestic food and industrial raw material needs while providing significant foreign

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<sup>17</sup> The Pension Act moved the administration of pensions from NAICOM to Pension Commission established to administer the Act.

<sup>18</sup> See analysis on legislative framework of the NII in Chapter Five.

exchange through exports'<sup>19</sup>. Now a major oil exporting country (and the biggest oil exporter holding the largest natural gas reserve in the whole of Africa)<sup>20</sup>, Nigeria imports most of its food items. Its growth rate and external position has been influenced by the 'evolution of the world market price for crude oil' The country's dependence on oil resulted in a decline in other income generating exports that existed before the oil boom of the 70s and the 80s. The oil and gas sector now accounts for about 90% of the country's GDP. This is ironic bearing in mind that Nigeria had been in petroleum production since 1958 with no significant contribution to GDP from the sector until 1972<sup>21</sup>.

Historically, Nigeria used to be an agrarian economy with 'a substantial mining sector'<sup>22</sup> which also exported cocoa, palm kernel, palm oil, rubber, cotton and groundnut<sup>23</sup>. In early independence, agriculture contributed about two thirds of the employment figures. This was disrupted by the civil war in 1966-1970 and all attempts by various regimes including a 'Green Revolution'<sup>24</sup> failed to return agriculture to its pre-war position<sup>25</sup>. The share of oil in the commodity exports increased from 0.2% in 1960 to 92% in 1986 while the figures for agriculture dropped from 80.9% to 4.5% in the same period<sup>26</sup>.

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<sup>19</sup> Ezeala- Harrison (n1) 193.

<sup>20</sup> World Bank Country Brief on Nigeria, 2  
<<http://web.worldbank.org/WBSITE/EXTERNAL/COUNTRIES/AFRICAEXT/NIGERIAEXTN/0..menuPK:368906~pagePK:141132~piPK:141107~theSitePK:368896.00.html>>accessed 40<sup>th</sup> april 2011.

<sup>21</sup> Ezeala- Harrison (n1) 193.

<sup>22</sup> ibid 194.

<sup>23</sup> ibid.

<sup>24</sup> Programme designed in the late 1970's to increase farm productivity through the distribution of fertilisers and seeds to farmers.

<sup>25</sup> ibid 195-6.

<sup>26</sup> ibid 198.

The oil boom saw government expenditure increasing while worsening the income and development differentials of rural and urban dwellers. A rural urban drift led to further abandonment of agriculture<sup>27</sup> in pursuit of white collar jobs. The sector remains undeveloped and there is a gradual winding up of industries due to poor infrastructure coupled with high cost of imported raw materials made worse by lack of local substitutes. Nigeria mainly exports crude oil and little effort is geared towards exporting of other goods and services as an alternative to oil. Rodrik had noted that a country which specialises in raw materials exportation but does not steer its economy into industrialisation will get ‘stuck in the periphery of the world economy’, become hostage to price fluctuations<sup>28</sup>. He therefore advocates for countries to push into modern tradable products to facilitate the paving of ‘a path towards convergence with the world’s rich countries’<sup>29</sup> as Asian countries like Japan and China had done.

The Nigerians Enterprise Promotions Decree often referred to as Indigenisation Decree of 1972 also contributed to the developmental challenges of Nigeria because it mandated the transfer of equity in foreign companies to indigenes. This marked the exit of foreigners from the domestic economic scene (including the NII) and the take-over of their shares by the federal government and a few wealthy Nigerians. Regrettably, ‘nationalisation of capital’ has the effect of ‘scaring away long-term investors’ and the unilateral dismantling of ‘foreign share-holding interests’ leads to loss of technical and management skills<sup>30</sup>. It also resulted in the dearth of technical

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<sup>27</sup> *ibid* 196.

<sup>28</sup> Dani Rodrik, *The Globalization Paradox: Democracy and the Future of the World Economy* (Norton 2011) 156.

<sup>29</sup> *ibid*.

<sup>30</sup> Uche (n6) 329.

skills and requisite capital to ensure growth in the NII and reduced the demand for insurance policies too<sup>31</sup>.

Nigeria has tremendous political and economic influence in West Africa being the largest trading nation with 60% of trade and GDP of the region<sup>32</sup>. However, the country's GDP figure of \$327,323million recorded in 2010 ranks 31<sup>st</sup> behind that of China, India, and South Africa which are rated 2<sup>nd</sup>, 4<sup>th</sup> and 25<sup>th</sup> respectively<sup>33</sup> globally.

Nigeria's developmental objectives since independence include 'the achievement of reasonable, non-inflationary economic growth, reduction of unemployment, regionally balanced development, development of high level manpower, the diversification of the productive base of the economy, and external balance'<sup>34</sup>. These objectives were enlarged to include privatisation and deregulation in the new millennium. Unfortunately all efforts towards these objectives have not brought desired results.

Recently, the country pursued very ambitious structural reforms in various sectors including the finance and telecommunications as a result of its return to democratic

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<sup>31</sup> Ade Ibiwoye et al, 'The Determinants of Life Insurance Consumption in Nigeria: A C0-Integration Approach' (2010) 2 IJAR 351,356.

<sup>32</sup> EU 'Nigeria and the European Union Trade for Development: An Introduction to Economic Partnership Agreement (2007) 9  
<[http://trade.ec.europa.eu/doclib/docs/2007/july/tradoc\\_135286.pdf](http://trade.ec.europa.eu/doclib/docs/2007/july/tradoc_135286.pdf)> accessed on 18 April 2011.

<sup>33</sup> IMF, World Economic Outlook Database.  
<<http://www.imf.org/external/pubs/ft/weo/2010/02/weodata/weoselser.aspx>> accessed 10/3/2011.

<sup>34</sup> T Ademola Oyejide and Abiodun S Bankole, ' Liberalisation of the Services Sector in Nigeria: Implications of Unilateral and Multilateral Approaches' (AERC Services Sector Liberalisation Conference, Nigeria, January 2001) 3  
<<http://siteresources.worldbank.org/INTRANETTRADE/Resources/ServicesNigeria.pdf>> accessed on 13 April 2011.

governance. In response to WTO Trade Policy Review (TPR) Report of 2005<sup>35</sup>, Nigeria noted that the reforms involved deregulation, privatisation, promotion of transparency and the ports and customs reforms. This included a ‘commitment to a market- oriented, private sector-led economy with government serving as a catalyst and providing the enabling environment for the private sector to thrive<sup>36</sup>’. Privatisation and commercialization policies were implemented by the Bureau of Public Enterprises (BPE) under the National Council on Privatisation (NCP)<sup>37</sup> to end inefficiencies and wastages of government owned firms.

The privatisation effort of government had among other things been geared towards reversing the effect of the Indigenisation Decree<sup>38</sup>. It encouraged private participation and foreign direct investment into the economy by selling off its equity in various sectors including insurance. In the NII, the government sold its equity in the two government firms that dominated the industry which are NICON Plc. and Nigeria Re. Nonetheless, desired growth and foreign participation remains an illusion. This confirms the fact that successful liberalisation requires more than change of ownership but regulations that correct market inefficiencies<sup>39</sup>. Besides, privatisation can only contribute to economic growth when preceded by ‘adequate legal and market institutions together with regulatory or competition framework’<sup>40</sup>. Furthermore,

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<sup>35</sup> WTO, ‘Trade Policy Review Report by Nigeria’ (2005) WT/TPR/G/147.

<sup>36</sup> *ibid* para 43.

<sup>37</sup> *ibid* para 48.

<sup>38</sup> Chibuikwe U Uche, ‘Government Ownership of Insurance Companies in Nigeria: A Critique’ (1999) 24 GPRI 216, 2 17.

<sup>39</sup> Mattoo A and Subramanian A, ‘India and the Multilateral Trading System After Seattle: Towards a Proactive Role’ (2000) World Bank Development Research Group Trade Policy Research 2379, 17 <<http://elibrary.worldbank.org/content/workingpaper/10.1596/1813-9450-2379>> assessed on 23<sup>rd</sup> April 2011; Mathur, Somesh K., ‘Multilateral Trading System and Developing Countries: Prospects and Perspectives with Special Reference to India’ (2002) *Jamia Millia Islamia*, 14.

<sup>40</sup> Joseph Stiglitz, ‘Globalisation and Its Discontents’ (Penguin, 2002) 56.

corrupt governments cannot successfully implement privatisation programmes because it would result in ‘briberization’ and government assets get sold off at below market price. Similarly, government ministers would appropriate more funds to themselves than to the government’s treasury<sup>41</sup>.

Attempt at infusing some transparency and accountability into the country to combat the systemic corruption hindering Nigeria’s development involved legal, institutional and administrative reforms in this regard. The legal instruments included the Independent Corrupt Practices and Other Related Offences (ICPC) Act and Economic and Financial Crimes Commission (Establishment) (EFCC) Act of 2002. They established the Independent Corrupt Practices Commission (ICPC) and the Economic and Financial Crimes Commission (EFCC) respectively. ICPC was combated corruption generally while EFCC dealt with economic and financial offences. Both Commissions are very active in holding officers of private and public organizations accountable for financial and other forms of impropriety and securing convictions in a lot of cases. Disappointingly, they have been criticised for being selective and hounding perceived enemies of the government.

The financial sector in Nigeria like other developing countries is dominated by commercial banks<sup>42</sup> and the financial sector reforms recorded limited success there with interest rates remaining high, while small and medium size enterprises do not have access to funds while ‘neglecting productive activities in the real sectors of the economy’<sup>43</sup>.

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<sup>41</sup> *ibid* 58.

<sup>42</sup> Maxwell J Fry, ‘In Favour of Financial Liberalisation’ (1997), 107 *The Economic Journal*, 754.

<sup>43</sup> WTO, ‘Trade Policy Review Report by Nigeria’ (2005) WT/TPR/S/147, para 89.

In the NII however, government policy of privatisation by divesting its majority shares in NICON and NigeriaRe recorded little impact on the sector. There ensued rancour between the NAICOM and the new owners of NICON about issues relating to non-injection of appropriate funds into NICON and non-payment of claims among other things. Thus the privatisation exercise brought no benefit to consumers but worsened situations. Therefore, NII remains largely underdeveloped with a myriad of problems despite increasing levels of supervision by NAICOM through annual guidelines and directives. The sector remains relatively small with poor underwriting capacity and low global ranking confirming Stiglitz's observations on privatisation without appropriate legal and market institutions<sup>44</sup>. For any form of reform to work effective legal and institutional structures are required. This thesis argues that the lack of appropriate laws and institutions account for the poor results from the last reforms. It therefore advocates for liberalisation of the NII to be effected by legal and institutional reforms in line with the GATS model.

Generally, the reforms did not record success in the economy as a whole since the moderate growth of 7.4% recorded between 2003 and 2009 in the economy was ascribed to rising oil prices. Poverty levels remain high with an estimated 70% of Nigerians still below poverty line. Growth in the non-oil sectors of the economy and a focus on human development programmes would be required for a reduction in poverty; this the insurance sector can effectively deliver.

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<sup>44</sup> Stiglitz (n40).

Insurance is an infrastructural service that also provides financial and social services which support entrepreneurial activities by reducing the effect of financial losses on business and families<sup>45</sup>. It mobilizes funds and supports viable businesses thereby improving the level of economic activities, employment figures and income and alleviating the problems associated with poverty. These include low incomes, deprivation of basic capabilities such as good healthcare, education and so on<sup>46</sup>. With insurance sector supporting economic activities in other sectors, the economy would experience growth and government is able to provide basic facilities and freedoms that improve on welfare generally.

This thesis argues for the liberalisation of the insurance sector as a catalyst for economic growth in Nigeria because it has the potential for facilitating growth and alleviating poverty. Though the emphasis has always been on the banking sector, Nigeria needs to focus on the NII because insurance services provide more economic and social welfare functions than the former. It only requires efficient and effective supervision and regulation to deliver.

This thesis aligns with Rodrik's<sup>47</sup> postulations that policies that target growth reduces poverty and policies that reduce poverty boosts overall economic growth<sup>48</sup>. In the same light, this study also acknowledges the importance of institution building for development by arguing that there is a need for 'complementary institutional and governance reforms' that ensure growth and poverty alleviation from trade openness and liberalisation. The study does not support entirely Rodrik's opposition to uniform

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<sup>45</sup> See discussion on Insurance functions in the Economy in s2.2.

<sup>46</sup> Amartya Sen, 'Development as Freedom' (Knopf Inc, 1999) 20.

<sup>47</sup> Who ironically is a leading critic of WTO and its impact on developing countries.

<sup>48</sup> *ibid.*

trade rules which he believes are made for the benefit of a few rich countries and which stifles ‘experimentation’ and ‘preclude potentially desirable policies’ and ‘heterodoxy in development strategies’<sup>49</sup>. Rather it argues that developing countries needn’t engage in long experimentation where the manpower and resources necessary for such are not usually available. Rather, regulatory principles and development strategies that have been tried, tested and found to succeed in various jurisdictions can be applied with little modification to fit the peculiarities of a country. As analysed later in chapter three, adoption of model laws and model clauses is a viable method of legal reform and liberalisation<sup>50</sup>. This is not intended as detailed legislation but as a ‘reference point or guide’ for a law reformer<sup>51</sup>. All that is required is flexibility in the adaptation of the model to the ‘local needs and circumstances’ of the country needing reforms.

This thesis therefore argues that Nigeria needs to strengthen its reforms in the NII through the adoption of the GATS model off liberalisation before more lock-in commitments to increase the benefits accruable from such bindings. Liberalisation done gradually would enable more efficient allocation of resources through competition when preceded by regulatory and institutional reforms. This envisages the development of effective regulatory mix of home grown rules using internationally recognised regulatory principles reflecting the peculiar situations of the NII<sup>52</sup>. More importantly, this thesis argues that the development of sound and

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<sup>49</sup> David Trubek and M. Patrick Cottrell, Robert Hudec and the Theory of International Economic Law: The Law of Global Space’ (Inaugural Conference of the Society of International Economic Law, Geneva Switzerland, July 2008)36.

<sup>50</sup> Rosa M. Lastra, ‘Financial Law Reform in Emerging Economies’ (2008) 23 JIBLR413, 417-18.

<sup>51</sup> *ibid* 418.

<sup>52</sup> Dani Rodrik. ‘How to Save Globalization From its Cheerleaders’ (2007) 1 Journal of International Trade and Diplomacy 1; Dani Rodrik, ‘Global Governance of Trade As if Development Really Mattered’ (2001) J F Kennedy School of Government, Harvard University.

effective regulatory authority is equally important for adequate prudential supervision and establishment of good corporate governance structures that ensure effective development and growth of the NII.

Therefore, the objectives for unilateral liberalisation and reforms of Nigeria are first to restructure the domestic insurance market for better efficiency and productivity and secondly to prepare the country for possible greater commitments within the GATS. This would increase the probability of reciprocal commitments and market access for its goods and services.

Nigeria is a labour intensive country especially in its insurance sector which would benefit from the export of surplus labour. However, to achieve market access for its labour in other countries Nigeria might need to undertake appropriate commitments in the GATS.

It is therefore imperative that the domestic landscape is well organised and regulated before further commitments in the GATS. Unilateral liberalisation alone would not bring about reciprocal commitments as would be discussed in chapter three. Nigeria would have to commit more gradually in the GATS to achieve market access for its export. However the first important step would be ensure effective legal and institutional infrastructure domestically.

These legal and infrastructural reforms would promote economic efficiency and growth and also create better opportunities for increased investment into the insurance services sector (both foreign and local). Nigeria's moderate commitment in insurance

services under GATS is unlikely to convince foreign insurance service providers that the government has long term commitments to its reform programmes especially given the manner in which foreign firms were expelled in the 1970's.

#### **1.4 STRUCTURAL CHALLENGES OF THE NII**

The NII is said to be one of the biggest insurance markets in SSA. In the year 2009, Nigeria was ranked 66<sup>th</sup> in the world behind South Africa, Morocco and Egypt which are 23<sup>rd</sup>, 51<sup>st</sup> and 57<sup>th</sup> respectively in terms of total premium volume<sup>53</sup>. In terms of premium generation in Africa, Nigeria is 4<sup>th</sup> while South Africa, Morocco and Egypt are 1<sup>st</sup>, 2<sup>nd</sup> and 3<sup>rd</sup> respectively. Regarding Insurance Penetration as a percentage of GDP, Nigeria is ranked 87<sup>th</sup> behind nine other African countries which include the three leading nations in Africa and other countries such as Kenya, Namibia, Tunisia, Algeria, Mauritius and Angola<sup>54</sup>. However, in terms of insurance density, Nigeria is ranked 87<sup>th</sup> behind all the countries listed above<sup>55</sup>. The insurance penetration and density figures are dismal in view of the abundant human and capital resources in Nigeria. Penetration figure of 0.5% recorded show that the industry contributes less than 1% to the GDP whereas the figures recorded for South Africa is 12.9% with most of the income from life insurance premiums.

The NII lacks resources to propel it to greater acceptability and sustainable growth<sup>56</sup>

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<sup>53</sup> Sigma Research, 'World Insurance in 2009' (Swiss Re Publications 2010) 31.

<sup>54</sup> *ibid* 37.

<sup>55</sup> *ibid* 36.

<sup>56</sup> Jide Akintunde, 'Burning Issues in Nigerian Insurance Industry' *Financial Nigeria* (Lagos, August 2010)

<[http://www.financialnigeria.com/development/developmentreport\\_category\\_item\\_detail.aspx?categoryid=16&item=173](http://www.financialnigeria.com/development/developmentreport_category_item_detail.aspx?categoryid=16&item=173)> accessed 10<sup>th</sup> August 2011; Oladele Ayeleso, 'Can Nigeria's Insurance Industry Regain International Confidence' *Nigerian Tribune* (Lagos, 22<sup>nd</sup> September 2010)

and this account for its low contribution to GDP in Nigeria. The quality enhancing elements required of most service industries for effective service delivery are missing in the NII. These are<sup>57</sup> ‘reliability’ which is the ability to perform service dependably and accurately; ‘responsiveness’ i.e. prompt service delivery; ‘competence’ which is the possession of required skills and knowledge; access i.e. approachability and ease of contact; ‘credibility’ which connotes trustworthiness and honesty; ‘security’ i.e. freedom from danger, risk or doubt; ‘assurance’ which is the ability to convey trust; ‘understanding’ i.e. making efforts to understand the customer’s need provision of caring and individualized attention to customers and ‘tangibles’ in terms of the appearance of physical facilities, equipment, personnel and communication materials.

This position is corroborated by NAICOM the NII regulatory agency which listed ‘weak insurance companies’, ‘poor compliance culture’, ‘inadequate legislative and legal framework’, ‘poor public perception of NAICOM as a regulator’ and ‘public resistance to insurance’<sup>58</sup> as part of the problems.

This thesis argues that liberalisation or greater openness preceded by adequate regulatory reforms will bring about a relaxation of trade restricting rules through the introduction of laws and regulations that offer more competition in the market<sup>59</sup> with

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<<http://tribune.com.ng/index.php/insurance/11373-can-nigerias-insurance-industry-regain-international-confidence> > accessed 10<sup>th</sup> August 2011; S.A. Aduloju, A. L Awoponle and S.A. Oke, ‘Recapitalization, Mergers and Acquisitions of the Nigerian Insurance Industry’ (2008) 9 The Journal of Risk Finance 449, 450.

<sup>57</sup> A Zeithaml Parasuraman and V A Berry, ‘A conceptual Model of Service Quality and Its Implications for Future Research’ (1995) 49 Journal of Marketing, 47.

<sup>58</sup> NAICOM, ‘NAICOM Corporate Strategic Plan 2011-2013’, <<http://www.naicom.gov.ng/index.php?p=NAICOM%20Corporate%20Strategic%20Plan%202011-2013>> accessed July 12 2011.

<sup>59</sup> Oyejide and Bankole (n34) 3.

little government intervention<sup>60</sup>.

Preliminary investigations<sup>61</sup> into the NII also confirmed that there exist a weak regulatory framework, sharp practices<sup>62</sup>, bad image and lack of trust<sup>63</sup> as a result of the perception of non-reliability and low level of awareness of consumers<sup>64</sup>. The pace of technological change is slow<sup>65</sup>. There are delays in claims payment, bad image, obsolete products and dishonourable practices. Other problems noticed are poor service delivery, poor human resource practices, low capacity, low insurance culture and over dependence on non-life business.

Low level of awareness of insurance benefits amongst Nigerians transcends the whole economy and advertisement campaigns and promotions have been ineffective in improving awareness or deliver a healthy growth to the NII. Most Nigerians do not recognize the need for insurance, a function of low literacy levels and a general risk taking attitude compounded with existing lack of trust for domestic insurance service providers. Consequently, the NII's sales record in personal insurance lines (PIL) is very low while most premiums are generated from corporate and governmental clients

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<sup>60</sup> *ibid.*

<sup>61</sup> The researcher had worked for over a decade in NII.

<sup>62</sup> Ayeleso (n56); Anthony Osae-Brown, 'Insurance: A Beleaguered Sector and Less than Penny Stocks' *Businessday* (Lagos, 6<sup>th</sup> June 2011).

<http://www.businessdayonline.com/NG/index.php/analysis/features/22592-insurance-a-beleaguered-sector-and-its-less-than-penny-stocks-> > accessed 15 August 2011.

<sup>63</sup> Ogeny Ejye Omar, 'The Retailing of Life Insurance in Nigeria: An Assessment of Consumers' Attitudes' (2007) *Journal of Retail Marketing Management Research* 41,46; Ayorinde (n85) 201.

<sup>64</sup> Carlos P Barros and Echika L Obijiaku, 'Technical Efficiency of Nigerian Insurance Companies' Technical University Lisbon WP018/2007/DE/UECE,5

<<http://pascal.iseg.utl.pt/~depeco/wp/wp182007.pdf>> accessed 1<sup>st</sup> August 2011.

<sup>65</sup> A Sulaiman, 'Nigerian Insurance Industry Today' (Faculty of Risk Management Seminar, Lagos, 1999); Pat Utomi, 'Environmental Factors and the Development of Insurance in Nigeria: Challenges of the Millennium' (International Insurance Summit, Abuja, 2000).

leaving untapped the potentials available from Nigeria's very large population<sup>66</sup>.

Delay in claims payment and compensation often occurs due to cash flow problems or insurers' inability to retrieve premiums from agents or brokers or some unnecessary internal bureaucratic bottlenecks. Compounding this problem is the poor sales from long term products like life and endowment policies denying the insurance firms of long term funds for investments or earning to meet short term obligations<sup>67</sup>. Similarly, new business development is also very low in the NII and traditional lines of insurance are sold with little or no modification. Insurers therefore engage in rate cutting and business snatching rather than developing individual clichés in the markets.

The problem with bad image is amplified by poor service delivery and unethical practices resulting from post-independence influx of indigenous firms into the NII. Poor Service delivery and claims settlement account for poor insurance penetration and credibility problems in the industry<sup>68</sup>. The public perception of the NII as an unreliable industry is justified partly by the nature of insurance and also corrupt practices worsened with the departure of foreign insurance firms<sup>69</sup>. There is preference for fake insurance policies because it is cheaper and the possibility of getting compensation in the event of a loss is slim with genuine ones. General lack of

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<sup>66</sup> R.O. Ayorinde, 'Insurance-Fund Investment Regulation in Nigeria' (2001) 20 JIR 195, 203.

<sup>67</sup> The NII is a predominantly non-life market and funds from such are usually not available for investment because they could be needed for short term settlement of claims. Sometime there could be cash flow and insurance firms resort to turn some of their investments to meet their immediate obligations.

<sup>68</sup> Ngozi Okereke, 'The Nigerian Insurance Industry – A Sectoral Rebirth' (Annual Education Conference of the Chartered Insurance Institute of Nigeria (CIIN), Lagos, 2007).

<sup>69</sup> Uche (n38) *ibid*.

trust in the NII directly affects productivity<sup>70</sup> and development of the sector. However, the liberalisation of the sector would attract domestic and foreign investment into the market coupled with superior skills, technology, systems which promote efficient and qualitative services. The challenges with under-capitalisation reducing retention capacity, the ability to hire and retain quality staff, and also product development would be allayed in the NII. This coupled with transparency associated with the GATS model would reduce corruption levels and clearly bring back some trust to the NII.

Corruption is an ill confronting all sectors of the economy which government has continued to battle with little success in the NII. It is established in literature that corruption has negative effects on growth and development and has a positive correlation with financial sector liberalisation<sup>71</sup> though most of these literatures are non-insurance subsectors of the financial sector. This thesis argues that there is little or no literature on the effect of corruption on a liberalised insurance sector. Rather, the sector has prevalent problems with fraud<sup>72</sup> i.e. corruption of fiduciary persons than with public officers<sup>73</sup>.

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<sup>70</sup> Omar (n63) 6.

<sup>71</sup> Keith Blackburn and Gonzalo F. Forgues-Pucio, 'Financial Liberalisation Bureaucratic Corruption and Economic' University of Manchester Center for Growth, Business-Cycle Research and Economics Studies Discussion paper 054, September 2005 < <http://www.ses.man.ac.uk/cgbcr/discussi.htm> > accessed 11<sup>th</sup> May 2012; Zvika Neeman, M. Daniel Paserman and Avi Sihmon, 'Corruption and Openness' University of Jerusalem Center for the Study of Rationality, Discussion Paper No.53 March 2004 < <http://ratio.huji.ac.il/dp/dp353.pdf> > accessed 11<sup>th</sup> May 2012; Geeta Batra, Daniel Kaufman and Andrew H.W. Stone, 'Voices of the Firms 2000' Investment Climate and Governance Findings of the World Business Environment Survey (World Bank Group, May 2002) < [http://socsci2.ucsd.edu/~aronatas/project/academic/voicesfirms2k\\_fulltext.pdf](http://socsci2.ucsd.edu/~aronatas/project/academic/voicesfirms2k_fulltext.pdf) > accessed on 11<sup>th</sup> of May 2010.

<sup>72</sup> Tajudeen Olalekan Yusuf and Abdur Rasheed Babalola, 'Control of Insurance Fraud in Nigeria: An Exploratory Study' (2009) 16 Journal of Financial Crime 4, 418; Jorg Schiller, 'The Impact of Insurance Fraud Detection Systems' (2006) 73 Journal of Risk and Insurance JIR 3, 421.

<sup>73</sup> Black's Law Dictionary Free Online Ed < <http://thelawdictionary.org/corruption/> > accessed 11<sup>th</sup> May 2012; Corruption usually involve public officers in breach of public trust, accepting or

Fraudulent practices in the insurance sector involves insurance companies conniving with brokers or other persons to inflate premiums or avoid liability of claims; brokers withholding premiums with the hope that no claim would be recorded; loss adjusters conniving with repairers or policyholders to make insurers pay claims for which they are not liable. These practices have had negative effects on the sector because it increases the cost of insurance and deprive legitimate claimants of compensation. This consequence is reflected both on the NII and the economy as a whole despite earlier regulatory reforms<sup>74</sup>.

Corruption is pervasive in Nigeria and it has been criminalised under various laws<sup>75</sup>. These laws deal with corruption generally and specifically in the financial sector<sup>76</sup>. However, because the level of corruption is a factor dependent on the possibility of perpetrators being caught corruption thrives in insurance in particular because of the lack of transparency in supervision and administration of the NII<sup>77</sup>.

The NII is an industry in ‘early growth stage’ with insufficient scale of insurable risks associated with the small size of markets, macroeconomic instability and market restrictions in form of government distortions which hamper efficient allocation of resources e.g. limiting entry of foreign suppliers into the market<sup>78</sup>. Therefore, the

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demanding bribes or using public offices to enrich themselves. There has been only one reported incidence of public officer’s corruption in recent years in the insurance industry relating to re-registration of insurance firms though corruption does exist in the bidding for the insurances of government assets.

<sup>74</sup> Yusuf and Babalola (n72) 419.

<sup>75</sup> This is in line with Chapter III of the United Nations Convention against Corruption (UNCAC) adopted by the General Assembly in its Resolution 58/4 on the 31 of October 2003.

<sup>76</sup> See discussion on EFCC Act in s1.3 above.

<sup>77</sup> See discussion on transparency in chapter six.

<sup>78</sup> USAID, ‘Assessment on How Strengthening the Insurance Industry in Developing Countries

Nigerian economy is yet to benefit from the growth potential of insurance services and this deny Nigerians of improved social wellbeing obtainable from the availability of quality insurance products that meet numerous economic and social needs.

There is need for the liberalisation of the NII to foster growth and development of the Nigerian economy. Liberalisation supported by effective legal and supervisory regimes can alleviate the problems of corrupt practices and restore confidence in the NII. Effective institutional and legal reforms, which create a strong independent and transparent supervisory body and regime, will facilitate easier detection of fraud and effective enforcement of sanctions. This would involve adopting international standards in practice, legislation and supervision, ethical and transparent operations, improving consumer awareness of insurance benefits and proper industry/market conduct<sup>79</sup>.

This thesis takes cognisance of the criticisms against liberalisation as a developmental tool such as its failure to deliver growth; increasing the levels of poverty and socio-political chaos in some developing countries<sup>80</sup>; it's being pursued at the WTO with a mind-set for market access at the expense of poverty alleviation; the inherent governance and accountability issues relating to principles of the WTO serving the interest of exporters from developed countries<sup>81</sup>; and that liberalisation provide very minimal economic linkages or benefits for most developing countries<sup>82</sup>. Furthermore,

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Contributes to Economic Growth' (2006) 10, <[http://pdf.usaid.gov/pdf\\_docs/PNADF482.pdf](http://pdf.usaid.gov/pdf_docs/PNADF482.pdf)> accessed 12<sup>th</sup> August 2011.

<sup>79</sup> USAID (n78) 8.

<sup>80</sup> Rodrik, 'How to Save Globalization' (n52) 9.

<sup>81</sup> *ibid* 10; Rodrik, 'As if Development Mattered' (n52); Stiglitz (n40).

<sup>82</sup> Robert O Keohane, 'Global Governance and Democratic Accountability' Chapter prepared for a volume to be edited by David Held and Mathias Koenig-Archibugi from the Miliband Lectures,

the inability of poor people in developing countries affected by policies to hold the WTO accountable together has led to the suggestion of a ‘global administrative law’ which would among other things promote accountability of ‘global administrative bodies’ such as the WTO in such a way that they meet the ‘standards of transparency, participation, reasoned decision, and legality’<sup>83</sup>.

This study also considered arguments relating to the inability of developing countries’ to have deep political and legal integration with the developed countries which results in the former settling for ‘second-best’ options in international economic convergence<sup>84</sup>.

However, while agreeing that the above scenarios occur in some sectors, this thesis argues that scholarly writing on liberalisation of financial services tend to concentrate on the banking and capital market mainly. Consequently, most of these criticisms stem from researches into the banking and capital market sector. This thesis emphasises the fact that insurance is not another capital flow sector but one that plays a uniquely positive role in the economy. The functions and operations of the banking and other sub-sectors in the financial sector are clearly different from those of the insurance sector. As would be demonstrated in chapter two, liberalisation of insurance services fosters growth and development and alleviates poverty in different aspects where adequate legal and institutional infrastructures are in place. Insurance supports other industries and sectors and improves the quality of life. More research is required

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London School of Economics, Spring 2002, 18

<<http://www2.lse.ac.uk/PublicEvents/pdf/20020701t1531t001.pdf>> accessed 10<sup>th</sup> May 2012.

<sup>83</sup> Benedict Kingsbury, Nico Krisch and Richard B. Stewart, ‘The Emergence of Global Administrative Law’ New York University Public Law and Legal Theory WP 10-1-05

<sup>84</sup> Rodrik (n52) 13.

before a conclusion can be drawn as to the applicability of the findings in the banking and other subsectors of the financial sector to the insurance industry.

This thesis further argues that there is a great deal of transparency within the WTO due to its effective rule setting and enforcing mechanism. It is principles and rules based thus ensuring participation of all members on equal basis through its fundamental principles such as non-discrimination, predictability, transparency and fair competition. It is also one of the very few international organisations where consideration is given to the developmental and growth needs of developing countries especially the poorest ones under its General System of Preferences (GSPs). Besides the WTO is the only international body till date 'to force US to change its policies'<sup>85</sup> thereby confirming its ability to tame world powers.

The WTO continues to provide an effective platform for trade negotiations between developing and developed countries and quite a number of developing countries have benefitted from this arrangement though some still find it difficult to do so. Therefore, condemning the WTO and other global economic integrations or convergence is not the key to economic growth and development in developing countries but finding ways of strengthening policies that ensure their success. If liberalisation is condemned, there are very negative economic circumstances that would result from protectionism especially for the poor developing countries.

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<sup>85</sup> For example, see Panel and Appellate Body report of *US- Tax Treatment for 'Foreign Sales Corporations'* WT/DS108/R and WT/DS108/AB/R respectively and subsequent enactment of the FSC Repeal and Extraterritorial Income Exclusion Act in compliance with the recommendations and rulings of the DSB; .Rodrik (n28) 79.

Furthermore, both protagonists and antagonist of the WTO have agreed that there are growth benefits from market openness. It is established in literature that this is achievable when done gradually, in proper sequence and preceded by adequate domestic institutions<sup>86</sup> and policies having a mix of imported trade rules and home-grown rules in tune with the specific situation of individual countries<sup>87</sup>. Similarly, scholars agree that growth does benefit the poor because of a correlation between growth and poverty alleviation<sup>88</sup>. However, the development of effective global administrative law if and when successful may provide an extra mechanism of ensuring greater accountability and governance in the WTO.

This study proposes that the application of GATS model for domestic regulation such as transparency, prompt authorization, reasonableness, objectivity and impartiality together with IAIS principles on effective supervision like corporate governance and prudential measures would reduce the incidence of insurance fraud and minimise unethical practices among insurance practitioners. Mechanisms (both legal and institutional) for the detection, investigation and sanctioning of fraudulent acts when in place would serve as a deterrent and reduce the incidence of fraud. This is accentuated by the creation of a transparent, independent and accountable supervisory body which administers the law pursuing the objective for the reforms which are proposed.

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<sup>86</sup> Aaditya Mattoo and Robert M. Stern, 'The Framework of Trade in Services: Overview' in Aaditya Mattoo, Robert M. Stern and Gianni Zanini (eds) *A Handbook of International Trade in Services* (OUP, 2008) 1.

<sup>87</sup> Rodrik, 'How to Save Globalisation' (n52) ; Rodrik, 'As if Development Mattered' (n52), UNCTAD, 'Trade and Development Aspects of Insurance Services and Regulatory Frameworks' (2005) Note on Ad Hoc Expert Meeting , UNCTAD/DITC/TND/2005/15, para 4 <[http://www.unctad.org/en/docs/ditctncd200515\\_en.pdf](http://www.unctad.org/en/docs/ditctncd200515_en.pdf)> accessed 23<sup>rd</sup> April 2011; .

<sup>88</sup> Rodrik (n52) 8; Rodrik 'One Economics Many Recipes' (n1).

Insurance liberalisation also involves the adoption of prudential regulatory practices such as risk and principles based regulations which ensure the efficient allocation of resources, proper risk management and risk control among insurers and the development of a financially sound sector that would provide sound insurance services to the economy. This is in line with World Bank's remark that "efficient, accessible, and simple regulations could unleash natural entrepreneurship for small and midsize firm in Nigeria"<sup>89</sup>.

Oyejide and Bankole however note that 'Nigeria's economy is largely open' ... but a further integration into the world trading system through the WTO framework would be more beneficial particularly to the services industry which has experienced a lull for over a decade'<sup>90</sup>. This study argues that the insurance sector is an oil sector alternative export capable of instigating growth in the Nigerian economy. There is need for greater liberalisation through legal and regulatory reforms modelled after the WTO/GATS which affords flexibility and progressive liberalisation mechanisms of service markets.

## **1.5 NIGERIA, TRADE RELATIONS AND THE WTO**

Nigeria engages actively in trade relations both within and outside its continent. It is an active and leading member of both the Economic Community of West African States (ECOWAS) an economic union of countries in West Africa, and the African Union (AU) the regional organization of African countries. Nigeria is also a front player in NEPAD which is an economic development programme initiative of African

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<sup>89</sup> World Bank Group's report on Doing Business in Nigeria 2010

<sup>90</sup> Oyejide and Bankole, (n34) *ibid*.

countries to develop Africa by Africans. Nigeria's membership of these organizations dates back to their inception<sup>91</sup>. Unfortunately, not much has been achieved from regional trade agreements (RTAs) especially in Africa where integration is not deep. The reality is that the benefits from multilateral liberalisation far outweigh those of regional liberalisation<sup>92</sup>.

Deeper integration involves 'behind the border' integration which requires the analysis of economic and political aspects of all non-border policies and practices like under the European Union (EU) and the North American Free Trade Agreement (NAFTA)<sup>93</sup>.

Failure of the African regional integration initiatives is directly related to the size and structure of African economies that manifest poor infrastructure which increases the costs of business<sup>94</sup> and results in 'higher consumer prices'<sup>95</sup>. African countries also lack adequate skills, manpower and 'multi-sectoral approach to trade facilitation'<sup>96</sup>. The continuous dependence of African countries on 'external markets for primary commodities' hinder intra-trade in the region<sup>97</sup>.

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<sup>91</sup> NEPAD website <http://www.nepad.org/> > accessed 12 August 2011.

<sup>92</sup> Marion Jensen & Yannick Vennes, 'Liberalizing Financial Services Trade in Africa: Going Regional and Multilateral' WTO Staff WP ERSD-2006-03, 9  
<[http://www.wto.org/english/res\\_e/reser\\_e/ersd200603\\_e.pdf](http://www.wto.org/english/res_e/reser_e/ersd200603_e.pdf)> accessed 23<sup>rd</sup> April 2011.

<sup>93</sup> Robert Z Lawrence, *Regionalism, Multi-lateralism, and Deeper Integration* (Brookings 1996) xviii

<sup>94</sup> Vivien Foster and Cecilia Briceno-Garmendia (eds) *Africa's Infrastructure: A Time for Transformation* (World Bank 2010) 146.

<sup>95</sup> Charles Abuka, 'Infrastructure, Regional Integration and Growth in Africa' in Jan Joost Teunissen and Age Akkerman (eds) *Africa in the World Economy - The National, Regional and International Challenges* (FONDAD and Hague, 2005)123

<<http://www.fondad.org/uploaded/Africa%20in%20the%20World%20Economy/Fondad-AfricaWorld-Chapter10.pdf>> accessed 20<sup>th</sup> April 2011.

<sup>96</sup> *ibid.*

<sup>97</sup> C Mutasa, 'Regional Integration and Debt in Africa: A Comparative Report of Africa's Regional Grouping' (2003) Afrodad Research Series, 5

<[http://www.sarpn.org.za/documents/d0000299/P295\\_Mutasa.pdf](http://www.sarpn.org.za/documents/d0000299/P295_Mutasa.pdf)> accessed 20th April 2011.

The unfavourable economic context for development of regional commitments such as severe macroeconomic disequilibria, foreign debt service burdens, lack of trade finance and overvalued currencies to mention a few<sup>98</sup> are also some of the problems. Furthermore, ‘costly overlapping memberships’<sup>99</sup> of multiple regional arrangements, ‘different time horizons for full liberalisation of trade’ and delay in implementation leave inhibiting tariff and non-tariff barriers in intra-regional trade among member states<sup>100</sup>.

Colonial alliances also affect the operations of the regional trade agreements in Africa. The objective of the ECOWAS agreement was to promote cooperation and integration leading to an economic union in West Africa<sup>101</sup> through the harmonization of policies and projects, liberalisation and abolition of custom duties and non-tariff barriers amongst member states thereby establishing a free-trade area<sup>102</sup>. However, these colonial alliances create rivalry between French and English speaking member states. Former French colonies formed an economic and monetary union known as the ‘West African Economic and Monetary Union (UEMOA from its French meaning)’ while the former British colonies established the ‘West African Monetary Zone

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<sup>98</sup> A Matthews, *Regional Integration and Food Security in Developing Countries* (FAO, 2003), Chapter Six < <http://www.fao.org/docrep/004/y4793e/y4793e0a.htm#bm10.2>> accessed 20<sup>th</sup> April 2011.

<sup>99</sup> Dima N. Sarbo, ‘The Challenges of Regional Integration in Africa: The Case of the Intergovernmental Authority on Development (IGAD)’ (2010) *Global Economic Governance Programme*, University College of Oxford, 25. < [http://www.princeton.edu/~pcglobal/conferences/GLF/sarbo\\_glf.pdf](http://www.princeton.edu/~pcglobal/conferences/GLF/sarbo_glf.pdf) accessed 20<sup>th</sup> April 2011.

<sup>100</sup> Mothae Maruping, ‘Challenges of Regional Integration in Sub-Saharan Africa: Macroeconomic Convergence and Monetary Coordination in Jan Joost Teunissen and Age Akkerman (eds) *Africa in the World Economy - The National, Regional and International Challenges* (FONDAD and Hague, 2005) 135 < <http://www.fondad.org/uploaded/Africa%20in%20the%20World%20Economy/Fondad-AfricaWorld-Chapter11.pdf>> accessed 22<sup>nd</sup> April 2011.

<sup>101</sup> Treaty of ECOWAS, Art 3.

<sup>102</sup> *ibid* subsection 2.

(WAMZ) for the purpose of creating a common currency called the 'Eco' to rival the CFA which is the currency of the former French colonies. Consequently, poor economic statistics coupled with lack of commitment and trust for each other has marred the level of accomplishment in the ECOWAS. To be effective as a regional economic block, there is need for effective regional infrastructure to foster operational regional institutions and build regional trust and unity<sup>103</sup>.

On the other hand, PTAs such as the EPA have always been negotiated on unequal basis leaving poor developing countries are at the mercies of developed countries such as the EU. Often times negotiations though having commendable objectives such as poverty alleviation and development gets entangled in non-trade related political issues <sup>104</sup> such as human rights<sup>105</sup>, terrorism<sup>106</sup>, disarmament, requirements for democracy<sup>107</sup> and international criminal justice<sup>108</sup> to mention a few. These become conditions for trade and aid. Furthermore, these PTAs tend to generally entail a higher level of conditions and commitments than those required under the GATS which simply is hinged on trade, market access, and development<sup>109</sup>. Generally, developing countries have limited resources to enforce preferential agreements often tilted against them in terms of benefits. Consequently, developed countries exercise overwhelming influence and power in the implementation of such arrangements<sup>110</sup>.

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<sup>103</sup> World Bank, 'Africa Infrastructure' (World Bank, 2010) 154-156

<sup>104</sup> EU ACP Economic Partnership Agreement (EPA) Art 8.

<sup>105</sup> *ibid* Art 9.

<sup>106</sup> *ibid* Art11a.

<sup>107</sup> *ibid* Art10.

<sup>108</sup> *ibid* Art11.

<sup>109</sup> Martin Roy, Juan Marchetti and Hoe Lim, 'Services Liberalization in the New Generation of Preferential Trade Agreements (PTAs): How Much Farther Than GATS (2007) 6 World Trade Review 155,

<sup>110</sup> Michael J. Trebilcock and Robert Howse, *The Regulation of International Trade* (Routledge, 3<sup>rd</sup> edn 2005) 492

The NEPAD on the other hand was originally intended as a home-grown economic development programme for Africa. Unfortunately, it has been designed by a ‘capitalist agglomeration’ having been concluded only after extensive consultations with leaders of the World Bank, IM, EU and some other transnational corporate executives<sup>111</sup>. Like the EU-ACP, this agreement contains intrusive conditions and has thus been termed a ‘weapon of control by international creditors’<sup>112</sup>. These and similar factors make regional liberalisation an unrealistic option for Nigeria hence the preference for the WTO/GATS framework where developing countries have been able to resist the hegemonic influence and power of developed countries like the USA<sup>113</sup>.

Though regional integration in services is relatively new<sup>114</sup> it does not preclude trade relations outside the region<sup>115</sup>. Therefore, active involvement in services trade relations with regional organisations has no negative effects on Nigeria’s involvement in multilateral trade relations outside the region.

Nigeria has been a member of the World Trade Organization (WTO) from inception having been part of the General Agreement on Trade and Tariff (GATT) since becoming independent in 1960. Though a part of the developing countries that

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<sup>111</sup> John K. Akokari, ‘The AU, NEPAD and the Promotion of Good Governance in Africa (2004) 13 Nordic Journal of African Studies 243, 247.

<sup>112</sup> *ibid.*

<sup>113</sup> Treblicock and Howse (n110) *ibid.*

<sup>114</sup> Rudolf Adlung & Peter Morrison, ‘Less than the GATS: “Negative Preferences” in Regional Services Agreements’ (2010) 13 JIEL 1103.

<sup>115</sup> Marion Jansen & Yannick Vennes, ‘Liberalizing Financial Services Trade in Africa: Going Regional and Multilateral’ WTO Staff WP ERSD-2006-03, 17

<[http://www.wto.org/english/res\\_e/reser\\_e/ersd200603\\_e.pdf](http://www.wto.org/english/res_e/reser_e/ersd200603_e.pdf)> accessed 23<sup>rd</sup> April 2011.

resisted the inclusion of services in the Uruguay<sup>116</sup>, Nigeria is a signatory to GATS. Services trade is a new area for which Nigeria has a low technical skill which accounts for its limited commitments in GATS. This thesis presents WTO/GATS as a liberalisation model for the NII that would enhance the potential for growth in the industry.

At the inception of GATS in 1994<sup>117</sup>, Nigeria made initial commitments in sectors such as Financial Services (not including insurance), Communication Services, Tourism and Trade Related Services and Transport Services. This was mainly for commercial presence and in natural persons only for the implementation of foreign investment. In the commercial presence there were limitations in the schedule which required 'foreign service providers (FSPs) to incorporate or establish the business locally' in accordance with Nigerian laws<sup>118</sup> but with only a 'maximum of 40 per cent equity participation' for financial services<sup>119</sup>. The composition of the board was required to reflect ownership structure' for same<sup>120</sup>. Foreign enterprises in Nigeria had the 'same rights and responsibilities' as domestic counterparts and could transfer their profits abroad in accordance with existing regulations<sup>121</sup>.

This schedule was amended in 1998 to include insurance commitments and a relaxation of earlier restrictions<sup>122</sup> especially with regards to financial services which

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<sup>116</sup> These are negotiations which began in Punta del Este, Uruguay and culminated in the creation of the WTO in 1995; see also our discussion on history of WTO in s3.1.2.

<sup>117</sup> GATS, 'Nigeria Schedule of Specific Commitments' (1994) GATS/SC/65, 5  
<<http://www.esf.be/pdfs/GATS%20UR%20Commitments/Nigeria%20SoC.pdf>> accessed 23<sup>rd</sup> April 2011.

<sup>118</sup> *ibid* 1.

<sup>119</sup> *ibid* 3.

<sup>120</sup> *ibid*.

<sup>121</sup> *ibid* 1.

<sup>122</sup> GATS, 'Nigeria Schedule of Specific Commitments Supplement 1' (1998) GATS/SC/65/Suppl.1  
<<http://www.esf.be/pdfs/GATS%20UR%20Commitments/Nigeria%20SoC%20Supplement%201.pdf>>

was scheduled under the ‘Understanding on Commitments in Financial Services’. The schedule relaxed equity restriction and allowed 100 percent foreigners equity in firms<sup>123</sup>. It further affirmed that the MFN treatment is accorded all countries while noting on-going negotiations in the West African regional association, ECOWAS where the Nigeria is a member. The schedule also confirmed that The Nigerian Investment Promotion Decree of 1995 guarantees against expropriation<sup>124</sup>.

The commitments in insurance services under financial services in the 1998 schedule under had the following General restrictions:

- (a) All government properties are to be insured with the National Insurance Corporation of Nigeria;
- (b) All imports into Nigeria to be insured locally by insurance companies registered in Nigeria.
- (c) An insurance broker has to obtain approval before entering into contract with foreign insurers.

For market access commitments in life, accident and health insurance, Nigeria was only bound in the commercial presence mode while unbound in all the other modes. In national treatment commitments under life, accident and health insurance, Nigeria had no limitations and was only bound in cross border and commercial presence mode while remaining unbound in other two modes.

For non-life insurances, Nigeria had no limitations on the cross border and

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<sup>123</sup> *ibid* 1.

<sup>124</sup> This could be construed as a plea by the Nigerian government that the mistake of 1972The Nigerian Enterprise Promotion Decree of 1972 popularly known as indigenisation decree would not be repeated.

commercial presence mode both for market access and national treatment commitments while it remains unbound in the other two modes of supply.

In the reinsurance and retrocession subsectors, Nigeria was unbound for national treatment commitments for presence of natural person's mode while it had no limitations in the other modes of supply. With regards to market access commitments for reinsurance and retrocession, there were no limitations on national treatment in the cross border supply and consumption abroad but Nigeria was unbound in the temporary entry of natural persons mode. For commercial presence, the limitations included a 20 percent compulsory cession and the right of first refusal for Nigeria Re before ceding to any reinsurer outside Nigeria. Furthermore, the establishment of reinsurance companies were subject to the approval of the Minister of Finance with consideration for the need to control the number of reinsurance companies in Nigeria in giving approval.

Nigeria has no limitations inscribed on its schedule for cross border supply and consumption abroad for reinsurance and retrocession<sup>125</sup>.

For services auxiliary to insurance such as broking and adjusting, no restrictions exists on market access and national treatment commitments for cross border, consumption abroad and commercial presence mode, though it remained unbound in the entry of natural persons mode in both.

Though Nigeria's commitment in GATS increased with its supplementary schedule in 1998, no amendment is recorded in thirteen (13) years despite greater internal

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<sup>125</sup> This position is reversed by NAICOM's directive of 2010, see discussion in chapter five s5.2

liberalisation in committed sectors. For example, the federal government of Nigeria no longer holds equity in NICON and had since reversed the policy which gave monopoly of insuring all government assets to NICON. On the negative side, Nigeria has increased its protectionist regime with the local content policy which requires a minimum of 40 percent local participation in all businesses relating to the oil and gas sector. Furthermore, the NAICOM Directives has introduced greater restrictions on cross-border buying of reinsurance services with its new guidelines<sup>126</sup>.

The NII is relatively open compared to other developing countries but her schedule of commitments under GATS does not reflect this because of the fact that Nigeria employs the mechanism of unilateral liberalisation<sup>127</sup>. The country requires more lock-in commitments in the WTO/GATS framework to give credibility to on-going reforms in the financial sector. Furthermore, Nigeria is yet to submit any offer in the current Doha negotiations which may be the opportunity for the country to 'correct the unfriendly and growth inhibiting environment of the country's services sector through lock-in of unilateral reforms that would facilitate the realization of its drive for enhanced foreign direct investment'<sup>128</sup>. This will also reassure trading partners of its commitment to progressive liberalisation of the NFS and NII particular.

Therefore, careful structuring of Nigeria's liberalisation programme and GATS commitments in line with the reform agenda being pursued by the country is significant. A concerted effort is also required to position the economy for growth

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<sup>126</sup> *ibid.*

<sup>127</sup> See discussion on unilateral liberalisation in Chapter three s3.1.

<sup>128</sup> Ademola Oyejide and Abiodun S Bankole, 'Gats and Nigeria: Dealing with Multilateral Services Negotiations within the Context of Unilateral and Development Objectives' (2005) Paper prepared for ILEAP Workshop on African Strategies for Bilateral and Multilateral Trade in Services Negotiations (Accra, Ghana March 9-12, 2005).

through the opening up of the NII through reforms of relevant laws and measures in line with the WTO/GATS model of liberalisation. This would facilitate effective liberalisation, a healthy NFS and vibrant NII for increasing participation of both domestic and foreign insurance service suppliers; improve skills, capacity and profit and the potential for growth of the economy.

## **1.6 CONCLUSION**

This chapter has revealed that Nigeria is a big country with enormous developmental challenges. It however argues that the NII has potential which can be accessed and harnessed for economic growth. It reviewed the structure of the NII and highlighted problems which have made reforms so far ineffective in the sector. These include ineffective unilateral liberalisation, weak regulatory and supervisory framework, unethical practices, and poor capacity among others. The chapter establishes that the current framework cannot enhance a viable NII and this deprives the economy of potential for growth. The thesis argues for the liberalisation of the NII to achieve its growth potentials in the economy. The next chapter would move away from the big picture and review literature on the nature and function of insurance sector especially with regards economic growth. It stresses the importance of regulation for a liberalised and competitive insurance market.

## **CHAPTER TWO**

### **INSURANCE SERVICES: REGULATION AND LIBERALISATION**

#### **2. INTRODUCTION**

The last chapter considered the developmental challenges of the Nigerian economy and the NII but argued that the industry had the potentials to contribute to the country's growth. It therefore concludes that the liberalisation of the NII is the key to economic growth and development in Nigeria. This chapter forms part of the contextual chapters of the thesis and it elaborates on the nature of insurance particularly to reveal the growth potentials and function of insurance services given the analysis of the NII in the previous chapter. It builds on the argument in the earlier chapter for the liberalisation of the NII and emphasises the importance of regulations and effective supervision for a successful liberalisation of the insurance sector while also noting the benefits and challenges attendant with it.

The analysis of the nature, regulation and liberalisation of insurance is made here because chapter one basically provided background information about the NII which is the big picture. It also presented the contextual framework of the study from the macroeconomic point of view and the NII in particular. This chapter therefore takes the analysis further to substantiate the argument in chapter one i.e. how economic and developmental goals are achievable with insurance liberalisation. Hence, emphasis is on adequate regulations to ensure effective competition, efficiency, growth and development of the insurance market.

The analysis is in six parts with the nature and role of insurance forming the first and second sections respectively. The third section examines the regulation of insurance bearing in mind the fact that liberalisation of insurance or any other service sector is critically dependent on domestic regulations while the fourth section presents and an analysis of regulations necessary for effective liberalisation. Section five examines the benefits and challenges of liberalisation of insurance while section six concludes with the argument that the benefits of liberalisation outweighs the challenges inherent in the process provided adequate legal and institutional infrastructures are in place.

## 2.1 THE NATURE OF INSURANCE

Though a definition of insurance is often avoided in laws because of the danger of leaving out some contracts in the process<sup>1</sup>, Birds offers one which is that

‘a contract of insurance is any contract whereby one party assumes the risk of an uncertain event which is not within his control, happening at a future time, in which event the other party has an interest, and under which contract the first party is bound to pay money or provide its equivalent if the uncertain event occurs’<sup>2</sup>

It is a contract between the insured and insurer where the former promises to indemnify the latter on the occurrence of certain mishaps stated in the insurance contract. Insurance is an infrastructural pillar of the society that ensures the survival of other sectors through risk management and provision of investment funds<sup>3</sup>. It is

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<sup>1</sup> John Birds, *Birds Modern Insurance Law* (8<sup>th</sup> edn, Sweet & Maxwell, 2010) 7; the same applies to laws in the NII.

<sup>2</sup> *ibid* 8.

<sup>3</sup> Mina Mashayeki, Elisabeth Tuerk and Deepali Fernandez, ‘Trade and Development Aspects of

both a ‘risk-shifting’ and ‘risk-sharing’ device<sup>4</sup> used by individuals and organizations to guarantee reimbursement on the occurrence of a covered event. Insurance contracts though a means of redistributing the financial costs of unexpected losses<sup>5</sup> are complex, legalistic, intangible and highly technical. They are also aleatory<sup>6</sup> but nonetheless a ‘business coupled with public interest’<sup>7</sup>.

Various legal and non-legal categorisations of insurance policies exist which include; First or Third Party Insurance; Life or other Insurances<sup>8</sup>; Social or Private Insurances; Retail or Corporate Insurances; direct Insurances or reinsurance<sup>9</sup>.

First party insurance involves individuals directly insuring their life or properties such as cars and houses while third party insurances are against future liabilities to others.

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#### Insurance

Services and Regulatory Frameworks’, in *Trade and Development Aspects of Insurance Services and Regulatory Framework*, UNCTAD/DITC/TNCD/2007/4, 5

<[http://www.unctad.org/en/docs/ditctnkd20074\\_en.pdf](http://www.unctad.org/en/docs/ditctnkd20074_en.pdf) > accessed 23<sup>rd</sup> April 2011; UNCTAD, ‘Report of the Ad Hoc Expert Meeting on Insurance Services’ (2006)

UNCTAD/DITC/TNCD/2006/1, para 4 <[http://www.unctad.org/en/docs/ditctnkd20061\\_en.pdf](http://www.unctad.org/en/docs/ditctnkd20061_en.pdf) > accessed 23<sup>rd</sup> April 2011; D. Konan & K. Maskus, (2004), Quantifying the Impact of Service

Liberalization In a Developing Country, World Bank Research WP 3913

<<http://elibrary.worldbank.org/docserver/download/3193.pdf?expires=1304834335&id=id&accname=guest&checksum=698DCA9624ECAB3FEC3F117E7E77A087> > accessed 10<sup>th</sup> April 2011; Pierre

Sauvé, ‘Completing the GATS Framework: Addressing Uruguay Round Leftovers’

Aussenwirtschaft, 57. Jahrgang (2002), Heft III, Zürich: Rüegger, S. 321

<http://www.cid.harvard.edu/cidtrade/papers/sauve/GATSLeftovers21.doc> 23<sup>rd</sup> April 2011.

<sup>4</sup> Harold D Skipper, ‘Liberalization of Insurance Markets: Issues and Concerns’ in Litan, Robert E., Paul Masson, and Michael Pomerleano (eds) *Open Doors: Foreign Participation in Financial Systems in Developing Countries* (Brookings 2001) 105.

<sup>5</sup> S K Sinha and Zaid Ahmad, ‘Global Financial Crisis – with Special Reference to Insurance Industry’ (2009) *African Journal of Marketing Management* 184.

<sup>6</sup> Aleatory contract because indemnity is paid by the insurer based on the chance of the insured risk occurring.

<sup>7</sup> The US Supreme Court in *German Alliance Ins. Co. v. Lewis*, 233 U.S. 389, 411-15 (1914); Susan Randall, ‘Insurance Regulation in the United States: Regulatory Federalism and the National Association of Insurance Commissioners’ (1999) *26 Florida State University Law Review* 625, 627; Harold D Skipper and Robert W Klein, ‘Insurance Regulation in the Public Interest: The Path Towards Solvent, Competitive Markets’ (1999) Center for Risk Management and Insurance Research, Georgia State University, Paper prepared for The Coordinating Committee on International Insurance Issues Coalition of Service Industries.

<sup>8</sup> Birds (n1) 3.

<sup>9</sup> Skipper, ‘Liberalization of Insurance Markets’ (n4) 106.

Usually, third party insurances are made compulsory by law as a form of socialization of insurance<sup>10</sup>.

Life insurance is often a long term insurance product that offers benefits for lives surviving beyond a certain period<sup>11</sup> or in the event of a person's death. It could also provide for disabilities, diseases or injuries. Some Life insurance policies like endowments compete with savings account products in developed countries and are often accepted as collateral for the extension of credit in the banking industry. Non-life insurance on the other hand indemnifies for loss or damage to properties such as houses, vehicles, business, and aircrafts and also for liability losses.

Social insurances are provided by government as compulsory public goods for satisfying some societal goals such as 'social equity'. Private insurances are mainly provided by private insurance companies and they aim at 'actuarial equity' whereby the premium reflects the expected value of losses.

Retail Insurances are policies for the benefit of individuals and they are also referred to as Personal Insurance Lines (PIL) when it is non-life insurance<sup>12</sup>. Corporate insurances like product liability, business interruption or group life often called commercial lines<sup>13</sup> in non-life are for the benefit of organizations.

Direct insurances are purchased by the public and non-insurance firms for a premium

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<sup>10</sup> Using insurance to solve social problems; Spencer L. Kimball, 'The Purpose of Insurance Regulation' (1961) 45 Minn. L. R 471, 506.

<sup>11</sup> Such as endowments, pensions or annuities.

<sup>12</sup> Skipper, (n4) 107.

<sup>13</sup> *ibid.*

while reinsurance is bought by insurance or reinsurance firms<sup>14</sup> which are within or outside particular jurisdictions. Reinsurance involves large risk exposures and is often written internationally. It helps in the geographical spread of risk in order that catastrophic losses are not concentrated in particular countries or regions. For example, the 911 losses were spread across all the continents of the world because of the operation of reinsurance. Liberalisation of trade in insurance services is vital for the economy to avoid systemic risk and financial crises<sup>15</sup> from catastrophic losses. Large insurance companies worldwide<sup>16</sup> conduct most of their businesses internationally through the geographical spread of risks while contributing to the insurance capacities of other countries.

## 2.2 ROLE OF INSURANCE SERVICES IN THE ECONOMY

Insurance, together with banking and securities are the central infrastructural sectors of the economy<sup>17</sup>. Legal scholars have not shown much enthusiasm for the research into the growth potentials of insurance. Rather, the focus has always been on banking services and securities market<sup>18</sup> because of the nature of insurance services. This

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<sup>14</sup> Reinsurance is second tier insurance which insures insurance firms or other reinsurers. Direct insurers re-insure part or sometimes the whole of risks written with reinsurers. The process is called ceding. Reinsurers also reinsure with other reinsurers through a process called retrocession.

<sup>15</sup> Systemic risk is discussed later in this chapter in s2.3.1.

<sup>16</sup> Like Swiss Re and Munich Re of Switzerland and Germany respectively.

<sup>17</sup> Juan Marchetti, 'Developing Countries in the WTO Services Negotiations' (2006) World Trade Organization Economic Research and Statistics Division, Staff WP ERSD 2004-06, 4 06

[http://www.wto.org/english/res\\_e/reser\\_e/wpaps\\_e.htm#2007](http://www.wto.org/english/res_e/reser_e/wpaps_e.htm#2007)[http://www.wto.org/english/res\\_e/reser\\_e/wpaps\\_e.htm](http://www.wto.org/english/res_e/reser_e/wpaps_e.htm) - 2004> accessed on 23<sup>rd</sup> April 2011.); UNCTAD, 'Trade and Development Implications of Financial Services' (2007) TD/B/COM.1/EM/33/3,17-18 <[http://www.unctad.org/en/docs/c1em33d3\\_en.pdf](http://www.unctad.org/en/docs/c1em33d3_en.pdf) > accessed 23<sup>rd</sup> April 2011. Konan and Maskus (n3) *ibid*.

<sup>18</sup> La Porta et al, 'Legal Determinants of External Finance' (1997) 52 *Journal of Finance* 1131; La Porta et al, 'Law and Finance' (1996), 105 *Journal of Political Economy* 1113; H. Spaman, 'Law and Finance Revisited' (2008) Harvard Law School John M Olin Centre Discussion Paper 12 <[http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=1095526](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1095526) > Downloaded 15<sup>th</sup> August 2011.

situation has kept hidden the positive correlation between insurance and the level of growth and development the reason developed countries have well-functioning insurance sectors compared to developing countries<sup>19</sup>. Before reviewing the growth dimensions of insurance, a brief analysis of its traditional role in the economy<sup>20</sup> is pertinent.

Insurance performs social and economic functions in the society by stabilizing ‘the finances of individual, families and organizations’ and indemnifying in loss situations thereby preventing financial destitution. It also has the unique function of encouraging ‘individuals and firms to specialise create wealth and undertake beneficial projects. The protection it affords enable entrepreneurs create and expand their business ventures. Being a pre-condition for the production and sale of many goods and services, insurance services also facilitates trade and commerce<sup>21</sup>. Many professions depend on insurance for survival through ‘credit risk transfers’ and financial confidence to embark on viable projects<sup>22</sup> which investor’s acquire. Insurance firms manage non-diversifiable risks of creditors and borrowers more efficiently than other financial institutions thereby providing credit<sup>23</sup> while also promoting the welfare and

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<sup>19</sup> Puri Laskshmi, ‘Introduction to the Trade and Development Aspects of Insurance Services and Regulatory Framework’ in *Trade and Development Aspects of Insurance Services and Regulatory Framework* (2007) UNCTAD/DITC/TNCD/2007/4, 1  
<[http://www.unctad.org/en/docs/ditctncd20074\\_en.pdf](http://www.unctad.org/en/docs/ditctncd20074_en.pdf)> accessed 23<sup>rd</sup> April 2011.

<sup>20</sup> Skipper, (n4) 19; UNCTAD ‘Trade and Development Aspects of Insurance Services and Regulatory Frameworks’ (2005) Note by Secretariat, UNCTAD/DITC/TNCD/2005/17, para 5  
<[http://www.unctad.org/en/docs/ditctncd200515\\_en.pdf](http://www.unctad.org/en/docs/ditctncd200515_en.pdf)> Accessed 23<sup>rd</sup> April 2011; Mashayeki, Tuerk and Fernandez (n3)6; Udaibir S.Das, Nigel Davies and Richard Podpiera, ‘Insurance and Issues in Financial Soundness’(2003) IMF WP/03/13, 8  
<<http://www.imf.org/external/pubs/ft/wp/2003/wp03138.pdf>> accessed 23<sup>rd</sup> April .

<sup>21</sup> *ibid.*

<sup>22</sup> Marijana Cuak, Sandra Loncar and Klime Poposki, ‘Insurance Sector Development and Economic Growth in Transition Countries’ (2009) 34 *International Research Journal of Finance and Economics* 29, 32; Marco Arena, ‘Does Insurance Market Activity Promote Economic Growth? Country Study for Industrial and Developing Countries’ (2006) 74 *JIR* 921.

<sup>23</sup> USAID, ‘Assessment on How Strengthening the Insurance Industry in Developing Countries Contributes to Economic Growth’ (2006) 10, <[http://pdf.usaid.gov/pdf\\_docs/PNADF482.pdf](http://pdf.usaid.gov/pdf_docs/PNADF482.pdf)> accessed 12<sup>th</sup> August 2011.

employment situation of families within the economy.

Insurance creates liquidity and facilitates economies of scale by ‘mobilizing savings from household sector and channelling them to corporate and public sectors’<sup>24</sup>. This helps develop the debt and equity market<sup>25</sup> and also encourages economic efficiency. It is pertinent to note that a positive correlation exists between savings and economic growth therefore, insurance also promotes economic growth in this manner. Similarly, insurance fosters efficient capital allocation<sup>26</sup> by making insurance funds available to ‘the soundest and most efficient firms, projects and managers’ through careful evaluation based on the substantial information gathered on risk profiles.

Insurers’ centuries of accumulated knowledge of risk makes them more efficient in the general management of risks<sup>27</sup>. They ensure proper pricing, better pooling and efficient transfer of risk to insurers or reinsurers. Insurance places the financial burden of risk on risk managers thereby reducing the total risk profile of the economy.

Insurance services improve the quality of individual life and increases social stability<sup>28</sup> with insurance policies on life, health, workmen and pension by providing compensation for dead or injured persons, (including accident victims) and their families. In doing this it relieves pressure on government budget<sup>29</sup> and public funds can be channelled into other beneficial projects. Finally, insurance provides contracts

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<sup>24</sup> *ibid.*

<sup>25</sup> USAID (n23) *ibid.*

<sup>26</sup> *ibid.*

<sup>27</sup> *ibid.*

<sup>28</sup> Mashayeki, Tuerk and Fernandez (n3) 6; Das, Davies and Podpiera (n20).

<sup>29</sup> Das, Davies and Podpiera (n20)8; UNCTAD (n20) *ibid.*

which help to hedge and diversify risks<sup>30</sup> and smoothen consumption in other areas.

In summary, insurance services are vital for social welfare and economic well-being through its use as ‘conduit of trade’, as ‘production inputs’, ‘income transfers’, and the ‘provision of socially relevant services’<sup>31</sup>. However, for a greater appreciation of insurance services it is important to examine the growth dimensions to the function of insurance in the economy.

This study strongly aligns with the Economic Growth Theory which is one of the prominent contemporary perspectives on development<sup>32</sup>. It focuses on the promotion of aggregate economic growth<sup>33</sup> and improving the economic statistics of the country<sup>34</sup>. The argument is that if insurance is liberalised, the growth functions of insurance yet to be experienced in the Nigerian economy would manifest and ultimately result in economic growth and development.

For conceptual clarity economic growth needs to be distinguished from economic development. Economic growth is commonly measured as the annual rate of increase in a country’s GDP<sup>35</sup>. It could be measured by ‘the growth of total output or of total

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<sup>30</sup> Xavier Gine, ‘Why does Access Matter? Impact on Growth and Poverty’ in Michael S. Kumar Barr and Robert E Anjali Litan (eds), *Building Inclusive Financial Systems : A Framework for Financial Access*, (Brookings 2006) 33.

<sup>31</sup> Rudolf Adlung, ‘The Contribution of Services Liberalisation to Poverty Reduction: What Role for GATS’ WTO WP ERSD 2007-01, 2-9  
<[http://www.wto.org/english/res\\_e/reser\\_e/ersd200701\\_e.pdf](http://www.wto.org/english/res_e/reser_e/ersd200701_e.pdf)> accessed 23<sup>rd</sup> April 2011.

<sup>32</sup> There are several theoretical perspective on law and development but the main ones identified are Modernization, Dependency, Welfarist, Feminist, Sustainable Development and Growth Theories; Kevin E. Davis & Michael J. Trebilcock, ‘Legal Reforms and Development’ (2001) 22 TWQ 21.

<sup>33</sup> *ibid.*

<sup>34</sup> The other perspectives on development have a social focus while economic growth focuses on income generation that has positive consequences on all social aspects.

<sup>35</sup> Philippe Aghion and Peter Howitt, *Economics of Growth*. (MIT Press 2009) 24

income'<sup>36</sup>. This is done by calculating either the GNP or GDP. The former being the calculation of total value of all income whether or not derived from within the country, while the latter is the total value of all income created within the country<sup>37</sup>.

Economic Development is broader because economic growth is just one of the parameters for its measurement. Development 'incorporates the diverse and broad aspirations of what might be called the "good life" in all its economic, social and political dimensions that each society sets'<sup>38</sup>. It is a 'qualitative change and restructuring in country's economy in connection with technological and social progresses'<sup>39</sup>. The main indicator of development is the 'increasing GNP or GDP which reflects 'an increase in the economic productivity and average wellbeing of a country's population' and 'it is closely linked with economic growth'<sup>40</sup>. However, 'economic growth and stability' is of 'greater concern in the developing world'<sup>41</sup> consequently, economic growth is employed as an indicator of economic development<sup>42</sup> in this study.

The criticisms by Sen on tackling the problem development from the economic development perspective and his idea of considering development from a wider perspective of real freedoms which are the ends of development is considered. This emanates from his belief that the success of a society is determined by the substantive

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<sup>36</sup> James M. Cypher, and James L. Dietz, *The Process of Economic Development*, (2<sup>nd</sup> edn, Routledge 2004) 31.

<sup>37</sup> *ibid.*

<sup>38</sup> *ibid* 47.

<sup>39</sup> Tatyana P Soubbotina, *Beyond Economic Growth : An Introduction to Sustainable Development* (2nd edn, World Bank Publications 2004) 141.

<sup>40</sup> *ibid.*

<sup>41</sup> Joseph E Stiglitz, José Antonio Ocampo and Shari Spiegel, *Stability with Growth :Macroeconomics , Liberalisation and Development* (OUP 2006)16.

<sup>42</sup> There are other indicators such human development index (HDI) which uses a wide array of complex index such as longevity, knowledge, standard of living' but they may be time consuming and the parameters under the HDI are not clearly developed. CIPHER and DIETZ (n36) 147.

freedom that the members of the society enjoy<sup>43</sup>. Therefore, violation of these freedoms results in ‘economic poverty’ which robs people of freedom to satisfy hunger’, achieves sufficient nutrition, obtain remedies for illnesses or deprive people of shelter, clean water and sanitary facilities<sup>44</sup>. Consequently, development has to be pursued not merely for income maximization but with consideration for the lives led and the freedoms enjoyed<sup>45</sup>. In essence development should encompass ‘economic freedom’, ‘political liberty’ and ‘civil freedoms’ and provision of means or access through such things like good education and health care system amongst others. This would involve making both procedural and substantive provisions for processes and opportunities for freedoms to be achieved by people.

This thesis agrees with Sen that the ends of development should be the improvement of the quality of life and that economic growth is not an end in itself but a means to achieving other socio-economic and political goals. It further argues that without adequate income, these freedoms may remain an illusion. Consequently, greater emphasis must be made on securing economic growth for the facilitation of desired societal freedoms. It is on this basis that this thesis pursues the goal of economic growth using a sector that provides social and welfare benefits together with known economic benefits.

Han *et al* studied the role of insurance companies in economic growth and found that insurance played a much more important role in the economies of developing

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<sup>43</sup> Amartya Sen, ‘Development as Freedom’ (Knopf Inc, 1999) 18.

<sup>44</sup> *ibid.*

<sup>45</sup> *ibid* 14.

countries than developed ones<sup>46</sup>. This complemented earlier studies of Outreville<sup>47</sup> and Enz<sup>48</sup> which had shown a positive relationship between the insurance development and economic development of developing countries. Han et al also affirmed that ‘economic growth is characterised by the soundness of a national insurance market’<sup>49</sup>. Aghion and Howitt also posit that economic growth is what ‘determines the material well-being of billions of people<sup>50</sup>, and accounts for why people in developing have poor and appalling living standards while those in developed nations live in a ‘style only a privileged few could have afford before the industrial revolution’<sup>51</sup>. Van den Berg and Lewer reiterated this view noting that ‘economic growth translates into very large differences in standards of living within just a generation or two’<sup>52</sup>. They assert that ‘a positive relationship between international trade and economic growth’ and declare that ‘no nation appears to have been ruined by trade’<sup>53</sup>.

Hoekman and Mattoo however found a positive association between service sectors efficiently run and economic performance. They posit that services ‘policy reforms will help reduce poverty – as sustained economic growth is the most powerful instrument to reduce poverty’<sup>54</sup>. However, Whalley reviewing various literatures on the benefits of service liberalisation has warned that some findings are theoretical in

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<sup>46</sup> Han et al, ‘Insurance Development and Economic Growth’ (2010), 35 GPRI 183,195.

<sup>47</sup> Francois J Outreville, ‘The Economic Significance of Insurance Markets in Developing Countries’ (1990) 57 JIR 487–498; Francois J Outreville, ‘Life Insurance Markets in Developing Economies’ (1996) 63 JIR 263.

<sup>48</sup> Rudolf Enz, ‘The S-Curve relation between per-capita income and insurance penetration’ (2000) 25 GPRI 396.

<sup>49</sup> Han et al (n46) 184

<sup>50</sup> Aghion and Howitt (n35)1.

<sup>51</sup> *ibid.*

<sup>52</sup> Hendrik Van den Berg and Joshua J Lewer, *International Trade and Economic Growth*. (M.E. Sharp 2006) 27.

<sup>53</sup> *ibid* 53-54.

<sup>54</sup> Bernard Hoekman and Aaditya Mattoo, ‘Regulatory Cooperation, Aid for Trade and the GATS’ (2007) 12 Pacific Economic Review 4, 402.

nature with no analytical underpinning linking it to growth<sup>55</sup> coupled with the fact that services were heterogeneous and the indices for measurement are usually varied. Nevertheless, Whalley did commend the work of Mattoo, Rathindran and Subramanian<sup>56</sup> as having strong econometric evidence in support of the assertion that openness in financial services market was strongly linked with high growth rates. This provides strong empirical evidence in support of the main theme of this thesis which is that insurance liberalisation portends increasing growth levels. It is however important that reforms precede liberalisation for the objectives economic growth to be achieved<sup>57</sup>.

This implies that a liberalised insurance industry requires the correct regulatory framework to push towards convergence with rich countries that trade in insurance services to contribute to economic growth. Consequently the next two sections discuss regulations and its necessity for liberalisation and economic growth in the insurance sector.

### **2.3 REGULATION OF INSURANCE AND ITS CHALLENGES**

Laws and government institutions are relevant to increase economic growth<sup>58</sup> and it is a critical priority in development efforts<sup>59</sup>. Not only for freer markets but ‘crucial for

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<sup>55</sup> John Whalley, ‘Assessing the Benefits to Developing Countries of Liberalisation in Services Trade’ (2003) NBER WP 10181, 44.

<sup>56</sup> Aaditya Mattoo, R Rathindran and A Subramanian, ‘Measuring Services Trade Liberalisation and its Impact on Economic Growth: An Illustration’ (2001) World Bank Policy Research WP 2655, 4-7  
<<http://elibrary.worldbank.org/docserver/download/2655.pdf?expires=1303562687&id=id&accname=guest&checksum=F647C4AF5823B29D266EB8542EEC8605>> accessed 23<sup>rd</sup> April 2011.

<sup>57</sup> Douglas Arner, *Financial Stability, Economic Growth, and the Role of Law* (CUP 2007) 28; This is the lesson learnt from the Asian and Latin American liberalisation efforts in the 1990s.

<sup>58</sup> Frank B Cross, ‘Law and Economic Growth’ (2001) 80 T LR 1737, 1739.

<sup>59</sup> Thomas F McInerney, ‘Law and Development as Democratic Practice’ (2004) 1 Voices Of Development Jurists, 4.

large scale national economic growth'<sup>60</sup>. Historically, 'the circumstances enabling growth were not inevitable but government is relied on for the creation of growth enabling conditions.'<sup>61</sup> Development of appropriate regulations was the enabling condition that brought about the Industrial Revolution and the economic growth that followed. In the same vein, for insurance services to perform its growth function, there is need to create enabling conditions with the appropriate laws for its regulation<sup>62</sup>. This implies that the appropriateness of regulations is contextual and relative to culture, history, socio-economic and political situations<sup>63</sup>. In the recent legal history of Nigeria, there has been series of reforms in the financial services sector which failed to achieve greater openness of the financial market. This study argues that better results would be accomplished with reforms using WTO/GATS model<sup>64</sup>.

Successful liberalisation of financial services (insurance services especially) require regulatory measures in place to protect the financial market<sup>65</sup>. Mattoo and Subramanian posited that credible policy of liberalisation require regulations that resolve market failures and pursue social goals with economic efficiency<sup>66</sup>. Similarly,

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<sup>60</sup> Cross (n58) 12.

<sup>61</sup> *ibid* 5.

<sup>62</sup> Marion Jansen & Yannick Vennes, 'Liberalizing Financial Services Trade in Africa: Going Regional and Multilateral' WTO Staff WP ERSD-2006-03, 3  
<[http://www.wto.org/english/res\\_e/reser\\_e/ersd200603\\_e.pdf](http://www.wto.org/english/res_e/reser_e/ersd200603_e.pdf)> accessed 23<sup>rd</sup> April 2011.

<sup>63</sup> Dani Rodrik, 'One Economics Many Recipes: Globalization, Institutions, and Economic Growth' (Princeton University Press, 2009) 2-3.

<sup>64</sup> Model discussed in chapter three and four.

<sup>65</sup> Mahmood Bagheri and Chizu Nakajima, 'Optimal Level of Financial Regulation Under GATS: A Regulatory Competition and Cooperation Framework for Capital Adequacy and Disclosure of Information' (2002) 5 JIEL 507, 517.

<sup>66</sup> Mattoo A and Subramanian A, 'India and the Multilateral Trading System After Seattle: Towards a Proactive Role' (2000) World Bank Development Research Group Trade, Policy Research WP 2379, 17 <<http://elibrary.worldbank.org/content/workingpaper/10.1596/1813-9450-2379>> assessed on 23<sup>rd</sup> April 2011 Mathur, Somesh K., 'Multilateral Trading System and Developing Countries: Prospects and Perspectives with Special Reference to India' (2002) *Jamia Millia Islamia* 14.

Mattoo and Stern<sup>67</sup> also noted the importance of the introduction of genuine competition, building of regulatory institutions that would provide solutions to market failures stressing that privatisation does not automatically translate to greater competition<sup>68</sup>. This is in consonance with IAIS statement that strengthening of regulation and supervision framework alongside slow and cautious liberalisation is essential for improving the efficiency of the market<sup>69</sup>.

This fundamentally reveals the importance of regulations for an efficiently liberalised service or insurance sector. The quality of an insurance market is a function of the effectiveness of the legal and supervisory structures. Likewise, liberalisation of the insurance sector requires effective domestic regulations to ensure its success.

Snyder predicting possible outcomes of the relationship between regulation and trade noted that 'free trade and domestic regulations could either be 'harmonized' or 'juxtaposed'. This either creates 'an open, competitive and well regulated insurance market' in the former or 'used for protectionist purposes to restrict foreign competition' in the latter<sup>70</sup>. This emphasises the importance of domestic regulations in the liberalisation process.

Rodrik on the other hand has noted that there is no 'one way' to prosperity while

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<sup>67</sup> Aaditya Mattoo and Robert M. Stern, 'The Framework of Trade in Services: Overview' in Aaditya Mattoo, Robert M. Stern and Gianni Zanini (eds) *A Handbook of International Trade in Services* (OUP, 2008) 1.

<sup>68</sup> *ibid* 17.

<sup>69</sup> IAIS, 'Guidance on Insurance Regulation and Supervision For Emerging Market Economies' (1997) Guidance Paper 1,5

<[http://www.iaisweb.org/\\_temp/Guidance\\_on\\_insurance\\_regulation\\_and\\_standards\\_designed\\_to\\_assist\\_supervisors\\_for\\_emerging\\_market\\_economies.pdf](http://www.iaisweb.org/_temp/Guidance_on_insurance_regulation_and_standards_designed_to_assist_supervisors_for_emerging_market_economies.pdf)> accessed 23<sup>rd</sup> April 2011.

<sup>70</sup> David Snyder, 'Free Trade in Insurance and Domestic Insurance Regulation—in Harmony or in Conflict?' (2007) 26 JIR 116.

countries should ‘have the right to protect their social arrangements, regulations and institutions’ as a matter of principles. In the same vein, no country has the right to impose their institutions on others therefore; organisations like the WTO should not interfere with domestic arrangements but lay down rules for managing the interface among nations in economic relations.

This thesis agrees with Rodrik’s principles but is quite adamant that global convergence and integration in insurance liberalisation is necessary because of the internationalisation of quite a number of insurance sectors especially transportation insurances and reinsurance. Consequently, trade-offs in domestic regulatory autonomy would become a necessary evil. In actual fact, traditional forms of insurance which had existed in African countries are inadequate and incapable of meeting the insurance needs of modern economies. Modern form of insurance did not originate in developing countries anyway so developed countries norms may be needed to participate in global insurance market through a reform and liberalisation process.

However, the functional context of regulation with regards to insurance services is discussed below.

### **2.3.1 Why Regulate in Insurance**

Regulation is a form of intervention which connotes different things depending on the context and the jurisdictions within which it is used<sup>71</sup>. The motives of regulations

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<sup>71</sup> Markus Krajewski, *National Regulation and Trade Liberalization in Services: The Legal Impact of General Agreement on Trade in Services (GATS) On National Regulatory* (Kluwer 2003) 1; Anthony I Ogus, *Regulation: Legal Form and Economic Theory*, (Hart 2004) 1.

may not be easily identifiable<sup>72</sup> sometimes because regulators engage in strategic manoeuvres to achieve ‘legitimate and sometimes illegitimate outcomes’<sup>73</sup>. Regulation is a ‘trans-disciplinary’ and ‘inter-disciplinary field of study’<sup>74</sup> and its theories range from the economic<sup>75</sup> to the non-economic ones<sup>76</sup>. The reason being that regulatory policies are dependent on the ‘economic, social and political circumstances in particular regulatory systems’<sup>77</sup>.

However, early scholars had noted that the goals of insurance regulation are solidity<sup>78</sup> and *Acquum et bonum*<sup>79</sup> which recently has been expanded to include consumer protection<sup>80</sup>, systemic stability, market confidence<sup>81</sup> and efficient operation of the insurance sector<sup>82</sup>.

Consumer protection which encompasses solidity and *Acquum et bonum* operates both on the macro level by protecting consumers against insolvencies of insurance companies and the micro level against losses from fraudulent market practices and

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<sup>72</sup> This is because the real reasons for some regulations may not be revealed e.g. Laws protecting domestic firms may be enacted under the guise of consumer protection.

<sup>73</sup> Cento Veljanovski, ‘Strategic Use of Regulation’ in Robert Baldwin, Martin Cave and Martin Lodge (eds), *The Oxford Handbook of Regulation* (OUP 2010) 99.

<sup>74</sup> Robert Baldwin, Martin Cave and Martin Lodge, ‘Regulation-The Field and the Developing Agenda’ in Robert Baldwin, Martin Cave and Martin Lodge (eds), *The Oxford Handbook of Regulation* (OUP 2010) 11-13.

<sup>75</sup> Economic theories on regulation are focussed mainly on market efficiency and market failure

<sup>76</sup> Such as the public interest theories focus on distributive justice’, paternalism i.e. justified interference with a person’s liberty for his welfare, good, happiness or needs; Gerald Dworkin, ‘Paternalism’ in Richard Wasserstrom (ed) *Morality and the Law* (Wardsworth 1971) 108.

<sup>77</sup> Krajewski (n71) 21.

<sup>78</sup> Spencer L. Kimball, ‘The Goals of Insurance Law: Means versus Ends’, (1962) 29 TJI 1, 20-29; solidity relates to the adequacy of insurance fund, and the preservation of its integrity together with its distribution to satisfy the needs for which it was collected; Kimball, ‘Purpose of Insurance Regulation’ (n10) 480-5; and ensuring accounts reflect both the actual and potential liabilities so that its solidity and solvency is assured at all times.

<sup>79</sup> Robert W. 80, ‘The Growing Sophistication of Solvency Policing Tools’ (2000) 19JIR 2, 238; *Acquum et bonum* states the moral obligations of insurers; Keaton, *Insurance Law: Basic Text*, (West Pub 1971) 2; this is reflected in equity, reasonableness, morality, fairness and Equality.

<sup>80</sup> This encompasses earlier two objectives.

<sup>81</sup> Rolf Nebel, ‘Regulations as a Source of Systemic Risk: The Need for Economic Impact Analysis’, (2004) 29 GPRI 2, 273.

<sup>82</sup> Laskshmi (n19) 2.

abuses<sup>83</sup>. Government provides regulations to address these problems bearing in mind the fact that consumers' lack an understanding of the complexities of insurance and are unable to assess the ability of an insurance company to perform its obligations in future<sup>84</sup>. The principle of solidity is manifested in all the post-independence law prescribing the type and mode of establishing insurance companies in Nigeria and regulating their investment behaviours. These are mandatory minimum paid-up capital, safeguard of funds, prescription of standards for account keeping and solvency margins respectively. There was also emphasis on the 'Nigerianisation (i.e. localization) of assets'<sup>85</sup> to ensure that all funds were invested locally.

Systemic stability requires a financial system that is free from risks that are capable of breaking down the entire domestic economic system<sup>86</sup>. Systemic risk causes disruption to flow of financial sector and has the potential of 'significant spillovers into the real economy'<sup>87</sup>. It manifests in the insurance industry as a result of weak insurance sector or from linkages with the banking or securities market<sup>88</sup>. Insurance sector systemic risk takes longer to manifest<sup>89</sup> therefore insurance regulation and supervision requires good surveillance mechanism for detection and management of

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<sup>83</sup> Lawrie Savage, 'Re-Engineering Insurance Supervision' (1998) World Bank Policy Research WP 2024, 111  
<<http://elibrary.worldbank.org/docserver/download/2024.pdf?expires=1318819414&id=id&accname=guest&checksum=F7EE419979B2897060BA9FD6AEA962B7>> accessed 12<sup>th</sup> April 2011.

<sup>84</sup> *ibid.*

<sup>85</sup> Ayorinde (n66) 202.

<sup>86</sup> Philip Bartholomew and Gary Whalen, 'Fundamentals of Systemic Risk' in George G Kaufman (ed) *Research in Financial Services: Banking, Financial Markets, and Systemic Risk*, vol 7 (JAI, 1995) 4.

<sup>87</sup> IAIS, 'Systemic Risk and the Insurance Sector' (October 2009) para 7 <[http://iaisweb.org/\\_temp/Note\\_on\\_systemic\\_risk\\_and\\_the\\_insurance\\_sector.pdf](http://iaisweb.org/_temp/Note_on_systemic_risk_and_the_insurance_sector.pdf)> accessed 12 April 2011.

<sup>88</sup> IMF, 'Evaluating Financial Sector Supervision: Banking, Insurance and Securities Markets' in *Financial Sector Assessment: A Handbook* (World Bank, 2005) 139  
<<http://www.imf.org/external/pubs/ft/fsa/eng/pdf/ch05.pdf>> accessed 12 April 2011.

<sup>89</sup> Unlike banks, the effects of systemic risk may take months or years to manifest.

potential and probable systemic risks. Failure may result in ‘insurance market capacity decline’ where insurers fail or there is a cluster of failed or insolvent insurance companies<sup>90</sup>. Efforts geared towards systemic stability in the NII are evidenced by regulations with various accounting and capital requirements together and sometimes directing compulsory re-registration of insurance companies<sup>91</sup>. The last exercise was the Insurance Directive of 2005 that increased share capital requirements of insurers and reduced their numbers from 107 to 49<sup>92</sup>. These efforts are geared towards weeding off weak and inefficient insurance firms.

Market confidence flows from systemic stability because confidence is dependent on the perception of stability by investors. With investor confidence, there is continuous inward flow of investment capital otherwise the market shrinks. One of the objectives of the insurance regulator is to ensure confidence in the insurance market to support continuous flow of investment for capital, growth and development in insurance sector.

Finally, efficient regulatory structures have been found to be a prerequisite for an efficiently operated insurance sector especially in context of insurance liberalisation and the evolving global insurance market<sup>93</sup>. Trends in the global market especially when it comes to technology, newer financial products and corporate failures have underscored the value of regulation in the insurance sector<sup>94</sup>. Optimum efficiency is

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<sup>90</sup> IAIS (n87) *ibid* para 24; G G Kaufman and E S Kenneth, ‘What is Systemic Risk, and do Bank Regulators Retard or Contribute to It?’ (2003) VII *The Independent Review* 3, 372.

<sup>91</sup> Insurance Decree of 1976, IA of 1991, 1997, and 2003.

<sup>92</sup> NAICOM, ‘List of Recapitalized Insurance Companies’  
<http://www.naicomonline.org/documents/Recapitalized%20Insurance%20Coys.%202009.pdf>  
accessed on 18<sup>th</sup> June 2009.

<sup>93</sup> Laskshmi, (n19) 2.

<sup>94</sup> *ibid*.

required to complete in the global insurance trade.

While the major objective of insurance regulation is to ensure the successful operation of insurance for consumer protection, other public policies reflecting pervasive attitudes influence the regulatory patterns in insurance<sup>95</sup>. These include democracy, socialization of risk, local protectionism and so on.

Democratization of insurance companies' management<sup>96</sup> ensures participation of shareholders in the decision-making of the organization through their appointed directors<sup>97</sup>. It also guarantees that only appointed directors take part in the management of the insurance companies.

Socialization of risk involves using insurance to provide social services like the Nigerian Motor Vehicle (Third Party) Act of 1945 which mandates third party insurance policies to cover legal liabilities of the owner in the event of injury or damage to property of third parties. Workmen's Compensation Act of 1987 also requires the provision of insurance against workplace injuries or death to employees. These laws make available compensation to individuals in the event of accident either on the highway or during the course of employment, thereby providing compensations which may not have been available without insurance.

Local protectionism is a political policy of subjecting foreign companies to

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<sup>95</sup> Kimbal, 'Purpose of Insurance Regulation' (n10) 502-10.

<sup>96</sup> Kimball, 'The Goals of Insurance Law' (n78) 22.

<sup>97</sup> *ibid.*

disadvantages in relation to domestic companies<sup>98</sup>. It plays a vital role in insurance law with conscious or unconscious discrimination<sup>99</sup> serving as handicap to the operation and development of the insurance industries<sup>100</sup>. In the extreme this may involve the complete elimination of foreign insurance companies' participation in local insurance business<sup>101</sup>. Protectionism often affects the establishment and participation of foreign firms in domestic market and this negates the WTO/GATS liberalisation framework requiring non-discrimination and national treatment<sup>102</sup>.

In the NII protectionist tendencies were found in the IA of 1961 that had discriminatory minimum share capital for foreign based insurance companies<sup>103</sup>. The mandatory incorporation of foreign companies, compulsorily cession<sup>104</sup>, insurance of all imports to Nigeria<sup>105</sup> in the NII and indeed the local content law<sup>106</sup> are all current protectionist regulations as would be discussed later on in chapter five. They continue to promote inefficiency in the NII and do not allow for effective competition from foreign suppliers of service. Consequently, there is no development in the NII making it the weakest link in the Nigerian financial sector.

Insurance regulation is basically for the protection of the consumer because regulatory goals like solidity, systemic stability, market confidence and efficient market basically are the macro-economic level protections for consumers. It is therefore imperative

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<sup>98</sup> *ibid.*

<sup>99</sup> Kimball, 'The Purpose of Insurance Regulation' (n10) 477

<sup>100</sup> *ibid* 506.

<sup>101</sup> Like the Nigerian Indigenisation Decree of 1972 .

<sup>102</sup> See discussion in s3.2.2.

<sup>103</sup> IA of 1961 s7 required 25,000 pounds for Nigerian companies and 50,000 pounds for foreign based insurance companies.

<sup>104</sup> Insurance Decree 1969.

<sup>105</sup> Insurance Decree 1976.

<sup>106</sup> Nigerian Oil and Gas Industry Content Development Act of 2010 s49 & 50

that insurance regulations serve public interest rather than private or special interests<sup>107</sup>.

This thesis argues that protectionism does not protect the consumer or the market rather it hurt consumers who are ‘penalized through high prices, lack of product innovation, and poor product choice’<sup>108</sup>. It however canvasses for liberalisation and greater openness of the NII so that the interests of the consumers would be protected rather than that of the ‘local protectionist interest groups’ in the insurance sector who stand to gain from trade barriers.

### **2.3.2 Insurance Regulatory Measures**

Following from earlier analysis on goals of insurance, the areas of regulation, approaches, instruments and strategies of insurance regulations are considered here.

Solvency and market regulations are the major areas of regulation in insurance<sup>109</sup>. Solvency regulations concern licensing, reports and financial analysis, capital requirements, on-site inspection, reserve regulation and other measures for early detection of potential insolvencies in order to prevent consumers’ suffering<sup>110</sup>. Market regulation involves approval of policy forms, agents and consumer complaints especially laws on unfair insurance contracts or claims processing. Rate regulations sometimes are addressed in regulations e.g. compulsory insurances are tariff based and regulated by NAICOM in the NII though it is becoming an unpopular form of

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<sup>107</sup> Skipper and Klein (n7) 11

<sup>108</sup> *ibid.*

<sup>109</sup> Emmet J Vaughan and Therese Vaughan, *Fundamentals of Risk and Insurance* (Wiley 10<sup>th</sup> edn 2008) 106.

<sup>110</sup> *ibid*

regulation.

However, regulatory approaches to the regulation of insurance services<sup>111</sup> include the competition emphasising approach which reflect minimal intrusion (like that of Chile and United States); the restrictive approach with emphasis on partial or complete sheltering of private insurers (such was in EU, Korea and Japan but now found only developing countries) and finally government action approach delegating the provision of insurance entirely to government (formerly practiced by China and India). The competition approach is the most agreeable to liberalisation because it encourages competition which the WTO/GATS model emphasises.

Regulatory instruments are the mechanisms employed in regulatory strategies for achieving insurance regulatory goals. These are Standards, Price Controls, Entry Controls, Public Ownership and Public Monopolies and Further Regulatory Measures<sup>112</sup>.

Standards are behavioural controls defining certain requirements which must be fulfilled to pursue an economic activity<sup>113</sup> and it includes target, performance and specifications standards<sup>114</sup>. Target Standards ‘imposes criminal liability’ for harmful consequences of a product<sup>115</sup> while performance Standard is an output control requiring fulfilment of quality conditions<sup>116</sup> at the ‘point of supply’<sup>117</sup>. The requirement of standard provisions in insurance contract and a fixed limit of liability

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<sup>111</sup> Skipper and Klein (n7) 16.

<sup>112</sup> Ogus (n71) 21-36.

<sup>113</sup> *ibid* 22.

<sup>114</sup> Anthony I Ogus, *Regulation, Legal Form and Economic Theory* (Clarendon1994) ch 9.

<sup>115</sup> Ogus (n71) 151.

<sup>116</sup> Krajewski (n71) 24.

<sup>117</sup> Ogus, (n71) 151.

for third party property damage is an example of performance standard. A specification standard is a form of input control which ensure the use or non-use of some specific elements<sup>118</sup>. Local content regulation<sup>119</sup> of Nigerian oil and gas industry specifying 40% minimum participation of local resources is an example of specification rules. Sometimes, rules of competition can also be referred to as standards because they prohibit particular ‘anti-competitive practices’ and also describe certain ‘behaviour which economic actors may not engage in’<sup>120</sup>.

Price control is a performance standard<sup>121</sup> aimed at the control of economic behaviour relating to price and the variants are actual price fixing controls or Fair Rate of Return (FRR)<sup>122</sup> and controls that set price at reasonable limits also called Historical Method (HM)<sup>123</sup>. Usually price control in insurance is in form of statutory instruments empowering regulators to fix prices<sup>124</sup> and rates on some insurance policies.

Price control is generally incompatible with liberalisation which requires minimally intrusive regulations that allow market forces determine price of goods and services<sup>125</sup>.

Entry Controls require authorization for new participants in a line of business and this could be qualitative or quantitative in nature or combined<sup>126</sup>. Qualitative entry controls prescribe qualitative prerequisites or qualifications while quantitative entry

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<sup>118</sup> *ibid.*

<sup>119</sup> Nigerian Oil and Gas Industry Content Development Act (2010).

<sup>120</sup> Krajewski (n71)24.

<sup>121</sup> *ibid* 25.

<sup>122</sup> Ogus (n71) 295.

<sup>123</sup> *ibid.*

<sup>124</sup> Krajewski (n71) 26.

<sup>125</sup> See s2.4.

<sup>126</sup> Krajewski (n71) 27.

controls are called prior approval, screening or licensing<sup>127</sup>. Two forms of qualitative entry controls identified are approvals relating to activities and approvals relating to use or marketing of objects<sup>128</sup>. Approvals relating to activities are commonly required for professionals in insurance management, broking or loss adjusting based on successful completion of an academic or practical programme<sup>129</sup>. These professionals may also require prior approvals. Entry Control is used mainly in the approval of new insurance products, licensing of new insurance service providers and general monitoring of insurance firms. It also supports liberalisation and ensures market efficiencies and growth. However, their use is moderated under the WTO/GATS liberalisation framework<sup>130</sup> due to some restrictive effects it may have on progressive liberalisation.

Public ownership which is often combined with public monopolies has been viewed as “the most complete and radical form” of regulation because it removes completely from private hands the means of production and eliminate the “inherent contradiction of forcing private interests to serve public goals”<sup>131</sup>. This is provided at local or regional levels alongside private providers thereby allowing for some form of competition. There are various forms of public ownership in practice<sup>132</sup>.

A hybrid of public ownership exists in form of public-private partnerships where public bodies cooperate with private investors in some areas<sup>133</sup>. The rationale for

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<sup>127</sup> *ibid.*

<sup>128</sup> *ibid* 27-8.

<sup>129</sup> Krajewski (n71) 28.

<sup>130</sup> GATS Agreement, Article XVI subsections (2) (a)-(f) examined in chapter three.

<sup>131</sup> Ogus (n71) 265.

<sup>132</sup> *ibid* 271-2; Krajewski (n71) 32.

<sup>133</sup> Krajewski(n71) 32.

public ownership or public monopolies as regulatory instruments varies<sup>134</sup> from its use as natural monopolies<sup>135</sup> or for the provision of public good. It may also be for distributional goals or simply “guaranteeing equal and affordable access” to these services which usually may include “cross-subsidization”<sup>136</sup>. This is akin to public service which has become an issue in services trade liberalisation<sup>137</sup>.

The public ownership instrument was adopted in the 1960’s by many developing countries like Nigeria which set up public corporations to provide a substitute for foreign suppliers following UNCTAD resolutions in 1972 and 1973<sup>138</sup>. It has since become outmoded in the last fifteen years giving way to deregulation, privatisation more importantly, liberalisation under the WTO framework. Nonetheless, it is pertinent to note that this strategy has the possibility of controverting liberalisation processes because of problems associated with discrimination against other providers<sup>139</sup>.

Other forms of regulatory measures identified by scholars include Information Regulation and Economic Incentives. Information Regulation often requires mandatory disclosures of price the identity, quality, composition or origin of the product.

Economic incentives are taxes, subsidies, charges, fees and even government

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<sup>134</sup> *ibid.*

<sup>135</sup> *ibid*; Ogus (n1 14) 267-70.

<sup>136</sup> Krajewski (n71 ) 33.

<sup>137</sup> See discussion on services in s3.2.1.

<sup>138</sup> UNCTAD Resolution 42/III of 1972 and 7/VII of 1973 encouraging LDCs to adopt import substitution strategies.

<sup>139</sup> The GATS allows direct action strategy only when provided on non-competitive and non-profit basis; see discussion on services s3.2.1(a).

procurement though sometimes some authors<sup>140</sup> disagree with their status as regulatory instruments because they do not involve rulemaking but Krajewski posited that they are because they are ‘aimed at influencing economic actors’<sup>141</sup>.

All the above instruments are engaged in various regulatory strategies in insurance but this section would only examine the five strategies often used in insurance regulation and their impact on liberalisation<sup>142</sup>.

The Command and Control (C& C) is the predominant form of strategy and this involves the enactment of laws prescribing acceptable standards and practices in the industry and sanctions for failure to meet such standards. It is the traditional forceful strategy which uses instruments such as standards setting, price control, entry controls and information regulations<sup>143</sup> to set acceptable standards while using criminal sanctions to back it up<sup>144</sup>. The Insurance Act 2003 of Nigeria and the Financial Services and Marketing Act of 2000 are examples of instruments used by Nigeria and the UK under a C&C strategy. Insurance liberalisation requires effective standard setting for the protection of consumers and market integrity thus the C & C is favourable to liberalisation under the WTO/GATS model<sup>145</sup>.

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<sup>140</sup> Giandomenico Majone, ‘From the Positive to the Regulator State: Causes and Consequences of Changes in the Mode of Governance’ (1997) 17 *Journal of Public Policy* 136, 148.

<sup>141</sup> Krajewski (n71) 33.

<sup>142</sup> There are eight regulatory strategies; command and control (C&C); self-regulation and enforced self-regulation; incentive based regimes; market harnessing controls; disclosure regulations; direct actions; rights and liabilities; public compensation or social insurance schemes. Baldwin and Cave (n74).

<sup>143</sup> Ogus (n76).

<sup>144</sup> *ibid* 36-9.

<sup>145</sup> This right to set standards is protected under GATS subject to conditions which are discussed under domestic regulations in chapter four.

Self-regulation strategy is the administration of self-imposed rules by trade associations or organizations which monitor and enforce them. It becomes ‘enforced’ when it is subject to government oversight or structuring<sup>146</sup>. Self-regulation was used as a predominant substitute for C&C strategy for years<sup>147</sup> in insurance services regulation but became outdated after the financial crisis of the 1990’s exposed its dangers<sup>148</sup>. For liberalising economies, self-regulation can only be used with government oversight knowing the tendency for self-serving regulations<sup>149</sup> to be contrary to the macro-economic goals of the country, contradict regulatory conditions for effective liberalisation<sup>150</sup> and violate existing obligations.

Other insurance regulatory strategies are the market harnessing controls strategy<sup>151</sup>, disclosure regulations and direct actions which involve the use of the instrument of government ownership, subsidies and franchising as a regulatory strategy. All these strategies are prominently used in combination with C&C strategy to protect consumers and the market. Direct action strategy was adopted in the 1960’s by many developing countries like Nigeria as part of their general import substitution strategy as earlier noted but is no longer in fashion.

Public compensation or social insurance schemes<sup>152</sup> are strategies that use insurance services to provide social welfare as noted in 2.1 above. This strategy could be

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<sup>146</sup> It is also called ‘meta-regulation’; B Hutter, ‘Risk, Regulation and Management’ in P Taylor-Gooby and J Zinn (eds) *Risk in Social Science* (OUP 2006) 215.

<sup>147</sup> In some cases centuries like The Lloyds.

<sup>148</sup> Liam Moloney, ‘Financial Services and Markets’ in Robert Baldwin, Martin Cave and Martin Lodge (eds), *The Oxford Handbook of Regulation* (OUP2010) 449; The Lloyds in UK lost its self-regulating powers in the wake of bankruptcy.

<sup>149</sup> Baldwin and Cave (n74) 39-41.

<sup>150</sup> Liberalisation within GATS has domestic regulation requirements chapter four s4.2.4.

<sup>151</sup> Simply is to harness market forces for control using such instruments as competition law, franchising and tradable permits.

<sup>152</sup> See discussion on role of insurance in s2.2.

juxtaposed with liberalisation of insurance services except when combined with direct action strategy which encourages discrimination<sup>153</sup>.

The review of insurance services regulatory strategies has revealed that these strategies are dynamic and change over time based on political and socio-economic factors of countries. This is evident especially with use of self-regulation and direct action strategies. It further revealed that not all these strategies support liberalisation and some may need some modifications to be able to support liberalisation. Finally, the C&C is the prominent of all the strategies and it is often combined with other strategies for effectiveness. However, these regulatory regimes, instruments and strategies sometimes fail to achieve the results for which they are designed. The next section examines some of these challenges and possible antidotes for an effective liberalisation program.

## **2.4 REGULATION OF INSURANCE FOR EFFECTIVE LIBERALISATION**

The liberalisation of services generally and especially under the WTO/GATS framework depends greatly on domestic regulations. Therefore, regulatory challenges often obstruct the achievement of growth and development in the liberalisation process. As noted by Stiglitz and others<sup>154</sup>, adequate legal structures are requirements for successful market openings. This section would therefore examine the factors that contribute to the inadequacies of regulatory frameworks for liberalisation such as lack of proportionality; distortion of competition; minimum capital requirements; and institutional inadequacy in supervision among others while considering means of

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<sup>153</sup> See discussion on services in s3.2.1(a).

<sup>154</sup> Joseph Stiglitz, *Globalisation and Its Discontents* (Penguin, 2002) 56; UNCTAD(n20); 'IAIS, Introduction, Insurance Core Principles and Methodology <[http://www.iaisweb.org/\\_temp/Insurance\\_core\\_principles\\_and\\_methodology.pdf](http://www.iaisweb.org/_temp/Insurance_core_principles_and_methodology.pdf)> accessed 9<sup>th</sup> October 2010.

resolving them to facilitate a viable insurance market. The argument is that effective regulatory infrastructures are required to ensure that the goals of liberalisation are achieved.

Regulatory effectiveness and efficiency requires that regulations must be proportional to the objectives for which they are made. The principle of proportionality connects ‘legal and economic assessments of a regulatory action’<sup>155</sup>. Without proportionality, regulations become unreasonable and burdensome and liberalisation will be ineffective. Proportionality test is an issue that legislative bodies need to resolve by anticipating economic effects of regulations before enactment<sup>156</sup>. Insurance regulators in their use of combination of strategies and instruments may end up with regulations lacking proportionality therefore becoming difficult to enforce.

Basically, a cost-benefit analysis is required to ‘balancing the cost and effect of a proposed regulations’<sup>157</sup>. This is a corollary of the proportionality test because a regulation is proportionate only if the ‘overall benefits exceed the overall costs’<sup>158</sup>. The Financial Services Authority (FSA) UK analyses the ‘direct costs of supervisory authority’, compliance cost (including the capital costs) of the supervised firms’ and ‘distortion costs, i.e. negative market impacts’<sup>159</sup>. A regulation which produces costs that outweighs the benefits is inefficient and lacks prudence.

Proportionality is one of the liberalisation principles used to ‘assess domestic

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<sup>155</sup> Nebel (n81) 274.

<sup>156</sup> *ibid.*

<sup>157</sup> *ibid.*

<sup>158</sup> *ibid.*

<sup>159</sup> *ibid* 276.

regulations under the GATS prudential carve-out provisions<sup>160</sup>. In the European Union (EU), ‘National restrictions are only justifiable if they are necessary, proportionate and not overlapping with the rules of country of origin’<sup>161</sup>. It is a component of the principle of regulatory adequacy which requires that regulations should be adequate enough to protect consumers and rectify market imperfections. Regulatory adequacy in insurance ensures that ‘quality, reasonably priced [insurance] products’ are available from ‘reliable insurers’ through adequate impartial, minimally intrusive and transparent regulations<sup>162</sup>. Regulations are adequate if they contain prudential regulations administered with regulatory effectiveness.

Adequate regulations would support a phased in liberalisation with a ‘maximum safe speed’ considering the fragility of the economy<sup>163</sup>. Regulatory impartiality connotes the application of regulations consistently and impartially to all competitors irrespective of nationality. This is similar to the National Treatment Principle<sup>164</sup> of the WTO/GATS framework of liberalisation. Minimum intrusiveness of laws involves limiting laws to those only justifiable in the public interest and placing more responsibility on the board of insurance companies to increase transparency and credibility of the regulatory process<sup>165</sup>. Transparency requirement involves public availability of all laws on the one hand and the regulator maintaining a realistic distance from insurers to avoid any form of ‘privileged association with regulators’. Foreign investors are not attracted to non-transparent jurisdictions because they require some certainty about their investments.

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<sup>160</sup> This is discussed in detail in chapter four.

<sup>161</sup> *ibid.*

<sup>162</sup> Skipper and Klein (n7) 22-29.

<sup>163</sup> *ibid* 22-5.

<sup>164</sup> See detailed discussion of National Treatment in chapter three and four.

<sup>165</sup> Skipper and Klein (n7) 26-9; like in principle based regulations discussed later.

The pursuit of adequate laws underscores the need for principled based regulations (PBRs) for effective insurance sector liberalisation. PBRs are outcome focussed regulations that concentrate on the goals and objectives of regulations rather than the processes. This is akin to performance based regulatory regimes<sup>166</sup> and it enhances sound market principles by integrating them into the supervisory activities and operationalizing their importance.<sup>167</sup> PBR is an important tool for pursuing Liberalisation programmes and this is emphasised by the WTO/GATS model<sup>168</sup>.

PBRs<sup>169</sup> could be formal<sup>170</sup> i.e. broadly worded principles or rules setting standards or substantive with regulatory conversations between the regulator and the regulated both of whom share the responsibility of interpreting the principles and rules while dispute resolution is through ‘consequentialist reasoning’<sup>171</sup>. Full PBR combines the characteristics of formal and substantive PBR and polycentric PBR is a form of full PBR which extends the network of interpreters to include trade unions, consultants and experts who may also monitor enforcement of the principles<sup>172</sup>. For the purpose of accountability and transparency, polycentric PBR is suggested for effective liberalisation. It is pertinent to note also that the key to the successful application of PBR is ‘high level of trust between all the participants in the regulatory regime’<sup>173</sup>. This is necessary to avoid the paradoxes inherent in the application of PBR regimes.

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<sup>166</sup> See discussion in 2.3.2.

<sup>167</sup> Martyn Hopper and Jenny Stainsby, ‘Principled-Based Regulation-Better Regulation’ (2006) 21 JIBLR 387-388.

<sup>168</sup> This model is discussed in chapters three and four.

<sup>169</sup> Julia Black, ‘Forms and Paradoxes of Principles Based Regulation’ London School of Economics and Political Science Law Society and Economy WP 13/2008.

<sup>170</sup> *ibid* 17.

<sup>171</sup> *ibid* 17-8.

<sup>172</sup> *ibid* 23-4.

<sup>173</sup> *ibid* 35-6.

PBRs therefore provide flexibility and facilitate innovation and ethical compliance culture thereby creating responsible organisations which organise their processes in line with the framework of regulatory principles.

Minimum capital requirement is another regulatory challenge to insurance services. It is a quantitative entry control often used in insurance regulatory regimes as a means of correcting some ‘market imperfections’<sup>174</sup> in the sector. Evidence has shown that fixed minimum requirements do not provide enough cushions against insolvencies<sup>175</sup> nor answers to the regulatory problems<sup>176</sup>. Furthermore, minimum capital standards do not cover all the risks of insurance firms<sup>177</sup> especially large multinational insurance companies that may come into the domestic insurance market as a result of liberalisation.

Currently, most countries applying principles based regulations have in operation Risk-based capital (RBC) or risk-based regulations (RBR) in replacement of minimum capital standards as quantitative controls. This is unlike developing countries like Nigeria which still maintain fixed minimum capital requirements as a regulatory strategy<sup>178</sup>.

RBR employs individual risk assessment of insurance firms to identify perceived high risk firms. These firms have high market shares and are ‘allocated significant

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<sup>174</sup> Terri M. Vaughan, ‘Financial Stability and Insurance Supervision: The Future of Prudential Supervision’ (2004) 29 GPRI 258,267.

<sup>175</sup> Klein (n80) 241.

<sup>176</sup> Vaughan (n174) 267.

<sup>177</sup> *ibid.*

<sup>178</sup> See discussion on legislative framework of the NII in chapter six.

supervisory resources' to avoid the damaging effect of the risk in the market<sup>179</sup>. The RBC has been increasingly applied by the National Association of Insurance Commissioners (NAIC) to various classes of insurers since 1992 in US<sup>180</sup>. In the UK, the FSA has the statutory duty of adopting policies that are 'proportionate, economically efficient and eligible to preserve competition, innovation'<sup>181</sup>. This framework enables flexibility and allows the FSA formulate rules and enforce them in a manner that is proportionate to the risks of each regulated firm<sup>182</sup>.

Risk based regulations require actions both on the policy and implementation levels<sup>183</sup>. On the policy level 'capital requirements must be linked directly to the firms risks' and explicit emphasis is placed on the responsibility of the board to manage risks with well documented policies highlighting the measures of doing so. This links the management of firms' risk with corporate governance. On the implementation level, prioritizing supervisory activities according to risks and emphasising preventive measures are germane.

Risk based regulations also involve risk based solvency capital which establish more meaningful 'minimum standards of capital adequacy related to an insurers risk of insolvency'<sup>184</sup> Fixed minimum capitals is an obsolete regulatory instrument that is giving way to risk based solvency and capital regimes.

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<sup>179</sup> Peter O Russell and Ian P Dewing, 'Towards the Integrated Prudential Supervision of UK Insurance: Further Implications for the Role of Actuaries and Auditors' (2004) 22 JIR 2, 6.

<sup>180</sup> Klein (n80) 241.

<sup>181</sup> Andromachi Georgosouli, 'The Nature of FSA Policy of Rule Use: A Critical Overview' (2008), 28 Legal Studies 1,127-128.

<sup>182</sup> *ibid* 128.

<sup>183</sup> Jeffrey Carmichael and Michael Pomerleano, *Development and Regulation of Non-Bank Financial Institutions* (World Bank Publications 2002).

<sup>184</sup> Martin Grac and Scott E Harrington, 'Risk-Based Capital and Solvency Screening: Hypotheses and Empirical Tests' Center for Risk Management and Insurance Research <<http://rmictr.gsu.edu/papers/RBCFASTm.pdf>> accessed on 18<sup>th</sup> March 2011.

Some regulatory instruments also result in inadequate capacity in the domestic insurance market because they distort market forces. The structure of the insurance industry can become unstable as a result of changes in the regulatory environment. Some regulations such as restrictive licensing and requirements which impede the access of new firms and products<sup>185</sup> have negative influences on liberalisation. This accounts for the low quality insurance products and higher premiums faced by developing countries that pursue protectionist strategies.

The implementation of regulations can also ‘exert anticompetitive effects’. High compliance cost eliminates smaller specialized firms while concentrating insurance business in the hands of a few<sup>186</sup>. Since insurance is easily traded across borders, national regulation is a determinant of the ‘overall competitive landscape’ of a country’s insurance sector<sup>187</sup>. Insurance regulations therefore require careful drafting and implementation to deliver growth and development.

Finally, one of the mundane challenges of insurance regulatory regimes is institutional inadequacies of the supervisory agency such as lack of independence and expertise.

The regulatory agency responsible for a viable, credible and stable insurance sector requires freedom from undue influences and knowledge of the operation of insurance services and its market. However, the increasing complexity of insurance markets has made insurance supervision and regulation complicated. Failures in markets of developed and even developing countries are evidences of inadequate regulatory

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<sup>185</sup> Nebel (n81) 276.

<sup>186</sup> *ibid* 277.

<sup>187</sup> Stijn Claessens, ‘Regulatory Reform and Trade Liberalisation in Financial Services’ in Aaditya Mattoo & Pierre Sauvé (eds) *Domestic Regulation and Service Trade Liberalisation*, (World Bank and OUP 2003) 129-146.

infrastructure<sup>188</sup> or regulatory failure.

The supervisory agency also needs to fulfil the conditions of efficiency, effectiveness and impartiality. Efficiency reflects in expeditious discharge of responsibilities, and prudent use of resources. The risk-based supervision is one of the current ways of guaranteeing supervisory efficiency. Effectiveness involves minimally intrusive means to ‘ameliorate market imperfections’, while impartiality connotes fairness in the treatment of all market participants.

Lack of supervisory independence is an enormous challenge to the regulation of insurance because of influences from various avenues. There are dire consequences for insurance markets without an independent regulator. Quintyn and Taylor<sup>189</sup> noted four significant dimensions of independence required for a financial supervisory body which are Regulatory, Supervisory, Institutional and Budgetary Independence.

Regulatory independence refers to the autonomy in setting technical rules and regulations within the confines of law while supervisory independence relates to licensing, supervision ‘*stricto sensu*’, sanctioning and crisis management<sup>190</sup>. Institutional independence requires the regulatory body to be ‘an institution separate from the executive and legislative branches of government’<sup>191</sup>. Budgetary

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<sup>188</sup> UNCTAD, ‘Trade and Development Aspects of Insurance Services and Regulatory Frameworks’ (2005) Note on Ad Hoc Expert Meeting, UNCTAD/DITC/TND/2005/15, para 80 <[http://www.unctad.org/en/docs/ditctncd200515\\_en.pdf](http://www.unctad.org/en/docs/ditctncd200515_en.pdf)> accessed 23<sup>rd</sup> April 2011.

<sup>189</sup> Mar Quintyn and Michael W Taylor, ‘Should Financial Sector Regulators be Independent?’ (2004) 32 Economic Issues <<http://www.imf.org/external/pubs/ft/issues/issues32/index.htm>> accessed 23<sup>rd</sup> April 2011; Mar Quintyn and Michael W Taylor, ‘Regulatory and Supervisory Independence and Financial Stability’, IMF WP/02/46, 14 <<http://www.imf.org/external/pubs/cat/longres.aspx?sk=15679.0>> accessed 23<sup>rd</sup> April 2011.

<sup>190</sup> Quintyn and Taylor ‘Regulatory and Supervisory Independence’ *ibid* 17.

<sup>191</sup> *ibid* 19.

independence connotes freedom from the executive or legislative interference in the size of budget, its use and salary structure or staff.

Lack of regulatory independence however is a function of weak public sector governance translating into weak regulatory framework, interference with supervisory process and poor enforcements which ultimately results in weak regulatory and financial sector governance<sup>192</sup>. Weak regulatory governance makes the regulator ineffective because it becomes encumbered by influences in setting technical rules. The nature and ‘internationalization’ of financial market<sup>193</sup> require that actions in one market may necessitate speedy action in others which may be difficult to achieve without effective independence. While crisis management may involve other government bodies, licensing and sanctioning ought to be left entirely with the supervisory body to deal with<sup>194</sup>.

Another institutional inadequacy of insurance regulation is lack of regulatory expertise. The quality of staff within the regulatory authority largely determines its regulatory effectiveness. It has been reported that ‘supervisory capacity is limited’ while many ‘supervisory agencies or departments are understaffed and lack essential skills’<sup>195</sup> in the SSA. Without skilled staff, there cannot be effective regulations hence the proliferation of obsolete regulations and poor performances of insurance markets in developing countries. Consequently, scholars in the area of regulatory capacity

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<sup>192</sup> Mar Quintyn, ‘Governance of Financial Supervisors and its Effect: A Stocktaking Exercise’ (2007) SUERF Studies 2007/4, 19-21 < <http://www.suerf.org/download/studies/study20074.pdf> > accessed 23<sup>rd</sup> April 2011.

<sup>193</sup> Financial markets have become part of a global network.

<sup>194</sup> Quintyn and Taylor ‘Regulatory and Supervisory Independence’ (n167) 17.

<sup>195</sup> Mar Quintyn and Michael W. Taylor, ‘Building Supervisory Structures in Sub-Saharan Africa- An Analytical Framework’ (2007) IMF WP/07/18, 13 < <http://www.imf.org/external/pubs/ft/wp/2007/wp0718.pdf> > accessed 23<sup>rd</sup> April 2011; Jansen and Vennes (n62) 9.

development have proffered national and regional solutions to the problem of inadequate regulatory capacity.

Quintyn and Taylor put forward five national models for meeting the capacity constraints of African countries. These include: the Singapore, UK, Irish, Bi-polar with supervision of bank separate, and Bi-polar with all deposit taking institutions in the central bank<sup>196</sup>. These models are based on the presumed power, capacity, independence and adequate resources that central banks possess in developing countries. The Singapore Model<sup>197</sup> unifies all financial sector supervision under the central bank. The advantage of this model is that there are no supervisory gaps and inter-agency issues are avoided. The supervision of non-bank sectors would benefit from the infrastructure, expertise, budget and independence of the central bank. The danger with this type of arrangement is that the central bank would become an extremely powerful institution.

The Irish Model<sup>198</sup> creates separate regulatory agencies but all sharing the infrastructure of the central bank. The advantage is that the agencies are separate institutions but share premises, data collection and staff with the central bank thereby benefitting from its 'logistical and budgetary support. The danger of conflict of interest in supervision is however inherent in this model.

The Bi-polar model that places banking supervision under the central bank<sup>199</sup> while regrouping other non-bank sectors in a newly established agency is the current South

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<sup>196</sup> Quintyn and Taylor 'Building Supervisory Structures in Africa (n195)22-6.

<sup>197</sup> *ibid* 22-3.

<sup>198</sup> *ibid* 24.

<sup>199</sup> *ibid* 24-5.

African model. The main advantage of this model is that the central bank is able to concentrate on the bank which is its key sector. The drawbacks of this model on the other hand are the challenges faced in creating a new agency with ‘appropriate governance structure and budgetary autonomy. This may be difficult in developing countries where such actions are often met with political inferences that ultimately affect the competence level of the agency. Furthermore, some deposit taking institutions which can affect the financial stability of the economy are left outside the supervision of the central bank.

The Bi-polar with supervision of deposit-taking institutions in the central bank<sup>200</sup> is the fourth model which is an improvement on the last model because all deposit taking institutions are kept under the control of the central bank. Nonetheless, the problem of establishing a new agency still exists for this model. The UK Model<sup>201</sup> unifies all regulators outside the central bank by creating a new institution from scratch. The advantages of this model is that it benefits from economies of scale, lack of regulatory gap and the pruning of the power of the central bank

Quintyn and Taylor however recommend for SSA the Irish Model with separate agencies sharing the infrastructure of the central bank or the Bi-polar model where all deposit taking institutions are supervised by the central bank and non-deposit taking financial institutions are supervised by a newly create agency. This thesis argues that the bi-polar with deposit taking institutions being supervised by the central bank would be suitable for NII having been successfully implemented in South Africa.

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<sup>200</sup> ibid 25.

<sup>201</sup> ibid 25.

Jansen and Vennes on the other hand suggested a regional supervisory structure solution which involves ‘the harmonization of regulatory framework and shifting some regulatory functions to the regional authorities’<sup>202</sup>. The problem with this arrangement is that fact that regional integration as noted in chapter one is not deep enough to allow encourage such a framework<sup>203</sup>.

The above examination of regulatory challenges of the insurance market especially within context of developing countries has revealed that insurance markets in developing countries including Nigeria basically require prudential regulations<sup>204</sup>. This will facilitate a viable insurance market<sup>205</sup> stabilize the sector, increase its potential for growth and protect policyholders<sup>206</sup>.

Prudential regulations are pre-conditions for liberalisation as evidence have shown that where they are not in place before financial market liberalisation, ‘countries have been more prone to exchange rate volatility and capital flight during periods of macroeconomic instability’<sup>207</sup>. This point is re-echoed by Sen and Rajan who warned on the need to strengthen domestic regulatory environment prior to and during liberalisation to forestall ‘calamitous consequences’ for the macro economy in the

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<sup>202</sup> Jansen and Vennes (n62) 9.

<sup>203</sup> This is discussed in chapter one.

<sup>204</sup> Note that prudential regulations is discussed here in the context of regulatory challenges of insurance sector. A detailed discussion of prudential regulations within the context of the WTO/GATS is discussed in chapter four.

<sup>205</sup> UNCTAD(n188) 21.

<sup>206</sup> UNCTAD, ‘Trade and Development Implications of Financial Services’ (2007) TD/B/COM.1/EM/33/3, 17-18<[http://www.unctad.org/en/docs/c1em33d3\\_en.pdf](http://www.unctad.org/en/docs/c1em33d3_en.pdf)> accessed 23<sup>rd</sup> April 2011.

<sup>207</sup> Julian Arkel, Insurance Developing Countries: Some Issues for Consideration’ in UNCTAD, *Trade and Development Aspects of Insurance Services and Regulatory Framework*’ (2007) UNCTAD/DITC/TNCD/2007/4, 316<[http://www.unctad.org/en/docs/ditctnecd20074\\_en.pdf](http://www.unctad.org/en/docs/ditctnecd20074_en.pdf)> accessed 23<sup>rd</sup> April 2011.

event of liberalisation<sup>208</sup>. This fact is reiterated by UNCTAD which notes that financial services reforms need appropriately designed regulatory and supervisory policies which adapts well to the specificity of each country to be effect growth<sup>209</sup>.

Developing countries desirous of growth and trade in insurance services need to adopt all these developed countries regulatory norms analysed above first, because these are the norms which have been become globally acceptable and has been found to promote market efficiency which is lacking in these countries. Secondly, these are the norms applied by developed countries with which trade is sought to promote growth and economic development. Thirdly, if not applied, developing countries would be incapable of competing globally in insurance services trade because of market inefficiency and as noted earlier, modern form of insurance is foreign to developing countries. Consequently, they have to play by the rules to benefit from its trade. Furthermore, regulations of domestic financial markets need a 'global functional approach'<sup>210</sup> and finally, these norms promote healthy growth and development of the insurance sector coupled with its positive effect on poverty alleviation and living standards of people.

## **2.5 LIBERALISING INSURANCE SERVICES: BENEFITS AND CHALLENGES**

Liberalisation of insurance is a *sine qua non* for ensuring a viable, competitive and solvent market for the benefit and interest of consumers and invariably the growth of

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<sup>208</sup> Rahul Sen, and Ramkishan S Rajan, 'Liberalisation of international trade in financial services in Southeast Asia: Indonesia, Malaysia, Philippines and Thailand' (2002) 4 Journal of International Financial Markets 170, 172.

<sup>209</sup> Mashayeki, Tuerk and Fernandez (n3) 16.

<sup>210</sup> Christian Tietje and Matthias Lehmann, 'The Role and Prospects of International Law in Financial Regulation and Supervision' (2010) 13 JIEL 6.

the economy. Burgess has shown that financial services can leverage economic development<sup>211</sup>. This is achieved through ‘improved productivity which facilitates domestic and international transactions’<sup>212</sup> and also financial services reform which is supported by well sequenced prudential regulatory and supervisory policies<sup>213</sup>. Where trade is restricted inefficiency is promoted amongst domestic providers of service. Hodges noted that the benefits of liberalising the financial sector include sharpening of competition; transfer of technology, broadening of the market, efficient resource allocation and enhanced downstream benefits such as lower prices, improvement in quality, and increase in variety of products and accelerated innovation within the market<sup>214</sup>. All these are indices of economic growth which aid development.

In designing a growth policy Aghion and Howitt had advised countries to take some six measures out of which fostering competition and liberalising trade are relevant to this study. Relying on empirical evidence, they posited that market competition and entry or threat of entry of foreign firms enhance growth because they force ‘firms to innovate in order to survive’<sup>215</sup>. The level of growth and innovation however is a function of the level of openness of each economy to entrance of foreign firms. They further stated that liberalising trade increases trade openness and market size while inducing ‘knowledge spillovers from more advanced to less advanced countries and

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<sup>211</sup> David F Burgess, ‘Is Trade Liberalization in the Service Sector in the National Interest’ (1995) 47 Oxford Economic Papers 60.

<sup>212</sup> UNCTAD, ‘Trade and Development Implications of Financial Services’, (2007) Commission on Trade in Goods and Services, and Commodities Expert Meeting on Trade and Development Implications of Financial Services and Commodity Exchanges Geneva, TD/B/COM.1/EM/33/3, 1

<sup>213</sup> UNCTAD (n188) para 4.

<sup>214</sup> James Hodge, ‘Examining the Cost of Services Protection in a Developing Country: The Case of South Africa’ (World Services Congress, Atlanta, November, 1999).

<sup>215</sup> Aghion and Howitt (n35) 267-279.

sectors<sup>216</sup>.

In essence, trade liberalisation would enhance market competition, by allowing foreign firms to compete with domestic firms thereby improving domestic productivity and growth. It ‘forces the most unproductive firms out of the domestic market’ and ‘domestic firms to innovate in order to escape competition with their new foreign counterparts’<sup>217</sup>. This confirms the fact that liberalisation is a vital key to economic growth.

Liberalisation prepares the platform on which to attain economic growth and provide the means to realize other developmental goals and freedoms. Without economic growth in terms of increasing GDP or GNP the realisation of development and other socio-economic and political policies of government will continue to be an illusion since they are dependent on adequate income. It would therefore be reasonable to focus this research on liberalisation.

This position is reinforced by results of studies which reveal that liberalisation of financial markets have led to tremendous economic prospects for a number of countries<sup>218</sup> and that ‘allowing foreign investors to transact in local securities does increase economic growth’<sup>219</sup>. Nash and Thomas<sup>220</sup> and other economists<sup>221</sup> also

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<sup>216</sup> Aghion and Howitt (n35) 376.

<sup>217</sup> *ibid* 377.

<sup>218</sup> Hodge (214); Mattoo, Rathindran and Subramanian (n56) 44.

<sup>219</sup> Geert Bekaerta, Campbell R. Harvey and Christian Lundblad, ‘Does Financial Liberalisation Spur Growth?’ (2005) 44 JFE 40.

<sup>220</sup> John Nash and Vinod Thomas, ‘Reform of trade policy: recent evidence from theory and practice’ (1991), 6 The World Bank Research Observer 219.

<sup>221</sup> Jeffrey D Sachs and Andrew Warner, ‘Economic Convergence and Economic Policies’ NBER WP W5039 < <http://www.nber.org/papers/w5039> > accessed on 22<sup>nd</sup> April 2011.

found similar results. Though Rodriguez and Rodrik<sup>222</sup> reported contrary findings triggering the idea that the relationship between liberalisation and economic growth is inconclusive<sup>223</sup>, recent studies have strengthened the theory that liberalisation brings growth. Chang, Kaltani, and Loayza<sup>224</sup> found a positive correlation between openness and economic growth with some level of complementary reforms aiding the result. Salinas and Aksoy<sup>225</sup> in their study of a number of developing countries that had liberalised in the last ten (10) years also found that trade liberalisation has increased levels of investment, export of goods and services and increased export diversification<sup>226</sup>.

Based on these empirical results, this thesis argues that regulations, liberalisation and economic growth are all inter-connected and liberalisation increases economic growth. It is important to stress though, that liberalisation and economic growth require a 'legal infrastructure' that can be created by legal reforms which 'adopt precise legal rules'<sup>227</sup>. That is why this thesis relies on the WTO/GATS model of liberalisation as a credible legal framework for liberalising the NII.

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<sup>222</sup> Francisco Rodriguez and Dani Rodrik, 'Trade Policy and Economic Growth: A Skeptic's Guide to the Cross-National Evidence' in Ben Bernanke and Kenneth S Rogoff (eds), *NBER Macroeconomic Annual* (MIT Press 2000) 60-62.

<sup>223</sup> Gozalo Salinas and Ataman Aksoy, 'Growth Before and After Liberalisation' (2006) World Bank Policy Research WP 4062, 2  
<<http://elibrary.worldbank.org/docserver/download/4062.pdf?expires=1303563416&id=id&acname=guest&checksum=0DEE3831EFA1377F8A11670F70FA0218>> accessed 23<sup>rd</sup> April 2011.

<sup>224</sup> Roberto Chang, Linda Kaltani and Norman Loayza, 'Openness can be good for Growth: The Role of Policy Complementarities' (2005) World Bank Policy Research WP 3763  
<[http://www-wds.worldbank.org/servlet/WDSContentServer/WDSP/IB/2005/10/31/000016406\\_20051031155510/Rendered/PDF/wps3763.pdf](http://www-wds.worldbank.org/servlet/WDSContentServer/WDSP/IB/2005/10/31/000016406_20051031155510/Rendered/PDF/wps3763.pdf)> accessed 22<sup>nd</sup> April 2011.

<sup>225</sup> Salinas and Aksoy (n223).

<sup>226</sup> *ibid.*

<sup>227</sup> Richard Posner, 'Creating a Legal Framework for Economic Development' (1998) 13 *The world Bank Research Observer* 1.

In liberalizing the insurance sector however, various scholars<sup>228</sup> have noted benefits as well as challenges. It is important that the challenges are identified and managed for the gains of liberalisation to accrue to a nation.

Liberalisation increases the number of insurance providers and cross border capital inflow<sup>229</sup>. This raises competition, efficiency in the allocation of resources and employment benefits which improve quality and standard of living. Secondly, the presence of more insurance companies especially foreign ones strengthen the domestic underwriting capacity by enabling the domestic insurance industry to take on large commercial risks which they may have been unable to write<sup>230</sup>. Global market credibility<sup>231</sup> also results from liberalisation making domestic market comparable to international markets and building the confidence of international investors in the domestic insurance industry. This alleviates the capital inadequacies hindering the growth of many small economies. Furthermore, a lot of improvement is experienced in market systems and activities<sup>232</sup> through infrastructures and technology transfer leading to 'gains in cost and efficiency. Consumers are able to get information on insurance companies and are better able to make informed choices when purchasing insurance products<sup>233</sup>. Similarly, new insurance products will result from technological development giving consumers a wider variety of products to choose from. Ultimately, the potential for economic growth is improved with the liberalisation of the insurance sector, because of increasing investment, capital inflow,

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<sup>228</sup> Jensen and Vennes(n62); Mashayeki, Tuerk and Fernandez (n3); Han et al (n202)189-195; Outreville 'The Economic Significance of Insurance Markets' (n47); Enz (48).

<sup>229</sup> Jansen and Vennes (n62) 4.

<sup>230</sup> Mashayeki, Tuerk and Fernandez (n3) 6 &15.

<sup>231</sup> *ibid.*

<sup>232</sup> *ibid.*

<sup>233</sup> *ibid* 14.

employment statistics, the contributions of insurance sector to GDP<sup>234</sup> and ultimately better living standards. This is the end goal which insurance liberalisation achieves.

Liberalisation also has well-known challenges especially amongst less developed countries whose economies are relatively small and may become vulnerable. Paramount amongst these is Infant Industry Argument<sup>235</sup> traceable to 19<sup>th</sup> century scholars<sup>236</sup> which states that countries in their early stages of economic development may require ‘an imposition of protective tariffs or quotas to allow infant industries’ develop. They argue that domestic firms may be unable to withstand competition from large foreign insurance providers. Another challenge is anticompetitive practices<sup>237</sup> such as ‘predatory pricing’ which may result in the ‘replacement of government monopolies with dominant insurance firms’. Further arguments relate to the possible compromise on the integrity of the sector which may result from mismanagement of funds and insurance market failures attributable to lack of effective control of foreign insurers by the weak regulatory framework. Developing countries often do not have the capacity in terms of human and financial capital to regulate the large foreign firms that may become part of liberalised domestic insurance market. As noted by UNCTAD, the regulatory capacity of African countries suffers from lack of techniques to deal with risk analysis and measurement and autonomy. They usually have small training budgets and their decisions are susceptible to political intervention. African insurance regulators in particular suffer

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<sup>234</sup> Han et al (n46)189-195; Outreville, ‘The Economic Significance of Insurance Markets’ (n47) ; Enz (n48) *ibid*.

<sup>235</sup> Neil McCulloch, L Alan Winters and Xavier Cirera, *Trade Liberalization and Poverty: A Handbook* (Centre for Policy Research 2001)234; Robert Hudec, ‘*Developing Countries in the GATT Legal System*’ (Gower, 1987) 159-60.

<sup>236</sup> Such as John Stuart Mill, *Principles of Political Economy* (Longman, Greene & Co, 1848) 922.

<sup>237</sup> UNCTAD ‘Trade and Development Aspects of Insurance Services and Regulatory Frameworks’ (2005) Note by Secretariat, UNCTAD/DITC/TNCD/2005/15, para 21  
<[http://www.unctad.org/en/docs/ditctnkd200515\\_en.pdf](http://www.unctad.org/en/docs/ditctnkd200515_en.pdf)> accessed 23<sup>rd</sup> April 2011.

inadequate application of information and communication technologies in supervision activities<sup>238</sup> and these pose a great deal of threat to the domestic economy when liberalised. It is therefore imperative that prudential regulations and supervisions are in place to ensure that firms do not act imprudently with the intense competition associated with liberalisation<sup>239</sup>.

This thesis submits that benefit of liberalisation far outweighs the challenges as evidence in both in theory and analysed empirical studies suggests that liberalisation of insurance facilitates growth when preceded with legal and institutional reforms. This thesis argues therefore that the liberalisation of the NII requires adequate regulations, a strong, independent and sufficiently funded supervisory agency.

## 2.6 CONCLUSIONS

This chapter has examined the nature of insurance services within the context of its function, regulation and liberalisation. It notes the regulatory challenges of developing countries especially in Africa and argues that liberalisation of the sector will increase its growth potential. The chapter concludes that an adequately regulated and effectively supervised insurance sector is a prerequisite for growth facilitating liberalisation. The next chapter would analyse the concept of liberalisation especially within the context of the WTO/GATS framework which is the model advocated for the reforms of the NII.

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<sup>238</sup> Israel Kamuzora, 'Insurance Services, Regulatory Frameworks In Africa and International Regulatory Standards' in *Trade and Development Aspects of Insurance Services and Regulatory Framework* UNCTAD/DITC/TNCD/2007/4, 63

<[http://www.unctad.org/en/docs/ditctnkd20074\\_en.pdf](http://www.unctad.org/en/docs/ditctnkd20074_en.pdf)> accessed 23<sup>rd</sup> April 2011.

<sup>239</sup> Masamichi Kono et al, 'Opening Markets in Financial Services and the Role of GATS' WTO Special Studies, 23<[http://www.wto.org/english/res\\_e/booksp\\_e/special\\_study\\_1\\_e.pdf](http://www.wto.org/english/res_e/booksp_e/special_study_1_e.pdf)> accessed 23<sup>rd</sup> April 2011.

## **CHAPTER THREE**

### **LIBERALISATION AND THE WTO FRAMEWORK**

#### **3. INTRODUCTION**

The last chapter dealt with the nature of insurance and revealed the growth functions of the sector in the economy while noting the importance of adequate and effective regulations in the development of a viable liberalised insurance sector. This chapter presents the context for the analysis of liberalisation within this thesis by examining the concept of liberalisation both in theory and within the framework of the WTO/GATS to justify its feasibility as a regulatory model for the liberalisation of the NII and other insurance markets in LDCs. This chapter discusses how GATS provides the parameters on which to model the regulation of the NII emphasizing the importance of the flexibility and progressive liberalisation in the model. It also notes the impediments that GATS may present to domestic regulations if cautious liberalisation is not done.

The two part analysis starts with a review of the concept of liberalisation especially within the framework of the WTO/GATS while the second part discusses the general framework of the GATS model for the liberalisation.

### 3.1.1 LIBERALISATION AND TOOLS

Liberalisation is the ‘process by which government takes action to move towards more liberal market’<sup>1</sup>. It is the ‘opening up of markets to the free flow of goods and services’<sup>2</sup> and it involves the ‘removal of legal and other barriers to competition’<sup>3</sup> while introducing a ‘competitive market environment’<sup>4</sup>. Liberalisation ‘connotes freeing up of restrictive conditions through the introduction of laws and regulations aimed at the ‘removal of government interference in financial and capital markets and barriers to trade’<sup>5</sup>. This may require ‘reduction of regulation or change of regulatory regime’<sup>6</sup>. Liberalisation and regulation are mutually reinforcing because liberalisation requires proper government regulation<sup>7</sup>.

Liberalisation can either be domestic liberalisation or international (i.e. trade) liberalisation. While domestic liberalisation aims at maintaining a competitive market for domestic actors, trade liberalisation aims to do the same for international actors<sup>8</sup>. Though they do not ‘necessarily coincide’ international or

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<sup>1</sup> Harold E Skipper, C V Starr and J Mack Robinson, ‘Liberalization of Insurance Markets: Issues and Concerns’ (2000) OECD Insurance and Private Pensions Compendium For Emerging Economies, 4 <<http://www.oecd.org/dataoecd/57/18/1815098.pdf>> accessed 22nd April 2011.

<sup>2</sup> Joseph Stiglitz, *Making Globalization Work* (Penguin, 2006) 15.

<sup>3</sup> Jan Wouters and Dominic Coppens, ‘GATS and Domestic Regulation: Balancing the Right to Regulate and Trade Liberalisation’ in Kern Alexander and Mads Andenas (eds) *The World Trade Organisation and Trade in Services* (Martinus Nijhoff, 2008) 209.

<sup>4</sup> Markus Krajewski, *National Regulation and Trade Liberalization in Services: The Legal Impact of General Agreement on Trade in Services (GATS) On National Regulatory* (Kluwer 2003) 4; T Ademola Oyejide and Abiodun S Bankole, ‘Liberalisation of the Services Sector in Nigeria: Implications of Unilateral and Multilateral Approaches’ (AERC Services Sector Liberalisation Conference, Nigeria, January 2001) 3 <<http://siteresources.worldbank.org/INTRANETTRADE/Resources/ServicesNigeria.pdf>> accessed on 13 April 2011.

<sup>5</sup> Stiglitz (n2) 59.

<sup>6</sup> *ibid* 5.

<sup>7</sup> *ibid*; regulation and its necessity for insurance liberalisation was discussed earlier in s2.4.

<sup>8</sup> *ibid*.

trade liberalisation often coincides or reinforces domestic liberalisation in practical terms especially in trade in services<sup>9</sup>.

Trade liberalisation is the ‘move toward freer trade through the reduction of tariff and other barriers’<sup>10</sup>. It presupposes the existence of some sort of barriers to trade which liberalisation aims to remove. Trade liberalisation is often a part of legal and economic reforms in most countries and an indispensable step for achieving trade openness<sup>11</sup> and globalization<sup>12</sup>.

Trade openness is a ‘powerful driver of economic growth’ that is crucial for poverty reduction and development<sup>13</sup>. This is not to mean that it is a ‘silver bullet for achieving development’ because other ‘institutional, macroeconomic, and microeconomic conditions’ together with ‘well designed social policies, must also be met to attain development’<sup>14</sup>.

Trade openness increases income and economic performance and also gives ‘firms and households access to world markets for goods, services, and knowledge, lowering prices, increasing the quality and variety of consumption goods, and fostering specialization of economic activity in areas where countries have a comparative advantage’<sup>15</sup>. Furthermore, it ‘generates more investment and fosters higher productivity of domestic industries as a result of competition and access to

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<sup>9</sup> *ibid.*

<sup>10</sup> Eddy Lee, ‘Trade Liberalization and Employment’ (2005 ) UN DESA WP 5,1  
<[http://www.un.org/esa/desa/papers/2005/wp5\\_2005.pdf](http://www.un.org/esa/desa/papers/2005/wp5_2005.pdf)> accessed on 15 June 2009.

<sup>11</sup> Neil McCulloch, L Alan Winters and Xavier Cirera, *Trade Liberalization and Poverty: A Handbook* (Centre for Policy Research 2001) xxi.

<sup>12</sup> *ibid* 5.

<sup>13</sup> UN Millennium Project Staff, *Trade for Development*, (UN Publications 2005) 1.

<sup>14</sup> *ibid.*

<sup>15</sup> *ibid* 32.

knowledge'<sup>16</sup>.

Therefore, within the context of this research, liberalisation would involve lowering or eliminating practices which affect the free flow of services between possible trading partners.

Trade liberalisation could take many forms; unilateral .i.e. autonomous or within the framework of bilateral or multilateral agreements. Unilateral or autonomous liberalisation is the form of liberalisation that attracts no form of reciprocity such as that being practised by the New Zealand trade policy since the 1980<sup>17</sup>. It can be pursued by countries either voluntarily or imposed externally as part of the conditionality of international financial institutions such as the World Bank or International Monetary Fund (IMF).

Unilateral liberalisation of trade and investment is undertaken by countries autonomously without a binding commitment in an international agreement<sup>18</sup>. It is also a means by which developing countries promote economic growth<sup>19</sup> and development without notifying or inscribing it in their schedules of commitment for fear of making it binding on them under WTO rules<sup>20</sup>.

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<sup>16</sup> *ibid.*

<sup>17</sup> Martin Richardson, 'Unilateral Liberalisation in a Multilateral World' (2001) University of German Alliance Ins. Co. v. Lewis, 233 U.S. 389, 411-15 (1914); Otago Economics Discussion Paper 0102, 4.

<sup>18</sup> Quamrul Alam, Mohammed Abdu Yusuf and Ken Coghill, 'Unilateral Liberalisation and WTO GATS Commitments: The Telecommunication Sector in Selected Countries' (2010) 24 Asian Pacific Economic Literature 43.

<sup>19</sup> Malcom Bosworth and Leanne Holmes, 'The WTO Doha Agenda- Progress and Issues for Asia Pacific Developing Economies' (2005) 19 Asian Pacific Economic Literature 55, 58.

<sup>20</sup> *ibid* 363.

Unilateral liberalisation nevertheless echoes progressive liberalisation goals of the GATS and this probably accounts for provisions in the agreement concerning the establishment of modalities for its treatment<sup>21</sup>. Members are only mandated to notify the Council for Trade in Services of ‘any changes to existing, laws, regulations or administrative guidelines which significantly affect trade in services covered by its specific commitments’<sup>22</sup> under the agreement. Therefore members are not obliged to notify in uncommitted sectors.

Conflicts have arisen over unilateral liberalisation because most service liberalisation in the world has been done unilaterally<sup>23</sup> outside the GATS and negotiations for the modalities on its treatment is being stalled in the current Doha round together with other service trade negotiations. The reasons adduced are the ‘hostage argument’ where service negotiations is said to be held hostage to stalemates in other sectors such as agriculture; lack of progress on some technical and rule making issues such as the emergency safeguard measures and the development of disciplines in all service sectors<sup>24</sup>.

Nonetheless, unilateral liberalisation functions in the best interest and for the benefits of the country alone. This is opposed to multilateral liberalisation where the benefits are for all the member countries of the multilateral organisation<sup>25</sup>.

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<sup>21</sup> GATS Art XIX:3.

<sup>22</sup> *ibid.* Art III:3.

<sup>23</sup> Phillipa Dee and Anne McNaughton, ‘Promoting Domestic Reforms Through Regionalism’ (April 2011) [http://crawford.anu.edu.au/pdf/staff/phillippa\\_dee/2011/Promoting\\_Domestic\\_Reforms\\_through\\_Regionalism.pdf](http://crawford.anu.edu.au/pdf/staff/phillippa_dee/2011/Promoting_Domestic_Reforms_through_Regionalism.pdf) accessed 13th May 2012; Byung-il Choi, ‘Treatment of Autonomous Liberalization in the WTO New Service Round’ (2001) 35 *JWT* 363-365.

<sup>24</sup> Markus Krajewski, ‘Service Trade Liberalisation and Regulation: New Developments and Old Problems’ in C. Herrmann and J.P. Terhechte (eds) *European Yearbook of International Economic Law* (Springer-Verlag Berlin Heidelberg 2010) 168.

<sup>25</sup> P. Dee, ‘Measuring the Impact of Alternative Strategies for Liberalisation, Deregulation and

Though no ‘similar exchange of commitments’<sup>26</sup> from other members is achieved in unilateral liberalisation, some ‘soft reciprocity’ may be recorded in forms of ‘non-trade-related benefits such as loans’<sup>27</sup>. Unilateral liberalisation is also driven by the prospect for large gains from cross-border trade and foreign direct investment<sup>28</sup>. Other reasons why developing countries opt for unilateral trade liberalisation include their perception that their service sectors are inefficient and uncompetitive and not able to withstand foreign competition. There is also the fear of being deprived of regulatory autonomy by multilateral commitment<sup>29</sup> which may affect the ability of their regulators to enforce national norms<sup>30</sup>.

Nigeria embarked on unilateral liberalisation exercises in the financial and other sectors of the economy through reforms<sup>31</sup> and Structural Adjustment Programmes (SAP)<sup>32</sup> in the early part the century and this has not achieved the desired goal of economic growth and development. This thesis argues the reforms were not successful because they were not benchmarked against any recognized standard or model. The efficiency of service liberalisation in developing countries does not only require the removing of trade barriers but also ‘instituting appropriate domestic regulatory framework’<sup>33</sup>. Though multilateral liberalisation is desired,

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Structural Reforms in Asia’ Background paper prepared for a study by the Asian Development Bank on Emerging Asian Regionalism: Ten Years after the Crisis, Australian National University, Canberra

<sup>26</sup> *ibid* 365.

<sup>27</sup> *ibid* 377.

<sup>28</sup> Bernard Hoekman, Aaditya Mattoo and Andre Sapir, ‘The Political Economy of Services Trade and Liberalisation: A Case of International Regulatory Cooperation’ (2007) 23 *Oxford Review of Economic Policy* 367, 358.

<sup>29</sup> Alam, Yusuf and Coghill (n18) *ibid*.

<sup>30</sup> Hoekman, Mattoo and Sapir (n28) *ibid*.

<sup>31</sup> See s1.4; WTO, ‘Trade Policy Review Report by Nigeria’ (2005) WT/TPR/G/147.

<sup>32</sup> Oyejide and Bankole (n4) 3.

<sup>33</sup> Aaditya Mattoo, ‘Developing Countries in the New Round of GATS Negotiations: Towards a Proactive Role’ (World Bank, March 2000), 3<

<http://ctrc.sice.oas.org/services/Articles/DCgats.pdf>> accessed 13<sup>th</sup> May 2012.

unilateral liberalisation for the purpose of enhancing efficient allocation of resources and competition in the domestic market is the first giant step forward. Multilateral commitments are easier to accomplish once this is in place.

Therefore this study is proposing the GATS model with adequate legal and institutional infrastructure in form of pro-competitive regulatory reforms as the standard for more effective liberalisation of the NII.

Bilateral liberalisation is an agreement between two countries to reduce barriers to trade between them with each getting reciprocal benefits from the other.

Multilateral liberalisation involves a lot of countries as it is done in WTO<sup>34</sup> and its goals are trade expansion and lowering of barriers to trade as evident in the preambles of the WTO and GATS Agreements. It is a liberalisation regime that seeks to benefit all member countries through the application of principles<sup>35</sup> which ensure equal treatment to all members. There are quite a number of other advantages of multilateral liberalisation over unilateral liberalisation. Multilateral trade agreements benefits from reciprocity and commitment<sup>36</sup>. Reciprocity ensures that ‘countries gain increased access to each other’s markets’ and ‘help avoid trade wars’<sup>37</sup>. Commitment on the other hand to a trade obligation in a multilateral liberalisation not only helps government locally to ‘stand up to protectionist interest groups’, on the international scene, it helps secure access to foreign

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<sup>34</sup> Liberalisation within the WTO is discussed later in s3.2.

<sup>35</sup> These principles are discussed in s3.1.2.

<sup>36</sup> Brian Copeland and Aaditya Mattoo, ‘The Basic Economics of Services Trade’ in Aaditya Mattoo, Robert M. Stern and Gianni Zanini (eds) *A Handbook of International Trade in Services* (OUP, 2008) 126-128.

<sup>37</sup> *ibid.*

markets while preventing arbitrary change of rules which may result in ‘hold-up’ problems<sup>38</sup>.

This thesis aligns with Hoekman’s view that developing countries ‘*have a great stake in a rule-based international system, which reduces the likelihood of being confronted with bilateral pressure from large trading powers to change policies that are not to their liking*’<sup>39</sup>. The study however argues that unilateral liberalisation is not entirely bad but could be used to correct some inadequacies in the domestic market and the preparation of the foundation for multilateral commitments.

Autonomous liberalisation does not secure reciprocal access while bilateral trade arrangements would not afford the broad platform for accessing a lot of markets. Consequently, developing countries seeking to liberalise for growth will need to negotiate market access with developed countries and other prospective trade partners on the broad platform of the WTO/GATS framework. Market access on a wide platform like WTO/GATS is required to allow competition and inflow of foreign investment capital and other benefits that guarantee economic growth.

### **Tools of Liberalisation**

Legal reform is a vital and paramount tool for trade liberalisation. It encompasses ‘everything from writing, or revising commercial codes, bankruptcy statutes, and company laws through overhauling regulatory agencies and teaching justice

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<sup>38</sup> *ibid.*

<sup>39</sup> Bernard Hoekman, ‘The WTO: Functions and Basic Principles’ in Bernhard Hoekman, Aaditya Mattoo and Philip English (eds) *Development, Trade, and the WTO* (The World Bank 2002) 43; see discussion on the intrusive nature of the bilateral agreements in chapter one s1.5.

ministry officials how to draft legislation that fosters private investment'<sup>40</sup>. It is effective in drafting regulations which emphasise competition and support a viable insurance market.

The process of legal reforms involves the following:<sup>41</sup>

- i) Creation or amendment of laws
- ii) Implementation of laws through rules and regulations by government agencies or regulator bodies.
- iii) Dissemination of legal information on how it is to be implemented to lawyers, government bodies, business community and other stake holders.
- iv) Effective enforcement and sanctions in cases of non-compliance
- v) Building of institutions that support the legal environment such as regulatory agencies and independent courts
- vi) Legal Education of lawyers and students in the new law and legal concepts
- vii) Judicial reforms to safeguard the independency of the judiciary or limit corruption
- viii) Establishment of alternative dispute resolution such as arbitration, mediation and conciliation

Legal reforms could include any or the combinations of “developing a home grown system”, “local adaptation of an existing foreign legal regime”, “reception of foreign law”, “adoption of model laws and of model clauses”, “harmonisation and other techniques of regulatory convergence” or the “adoption of international

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<sup>40</sup> Richard E. Messick, ‘Judicial Reform and Economic Development’ (1999) 14 The world Bank Research Observer 117.

<sup>41</sup> Rosa M. Lastra, ‘Financial Law Reform in Emerging Economies’ (2008) 23 JIBLR413, 415.

financial standards”<sup>42</sup> which this thesis canvasses.

There exist differences in the effectiveness of reforms from one country to another depending on the degree of efficiency of the judiciary<sup>43</sup>. Consequently, ‘a great deal of work is required to design laws that are actually enforceable in most developing countries, particularly those with a history of poor enforcement of rules and laws’. The mere copying western laws without effective local adaptations may lead to ineffective legal reforms.

Despite the fact that the efficacy of legal reforms is challenged in various empirical studies<sup>44</sup>, developing countries need reforms to improve the quality of institutions responsible for enacting and enforcing laws and regulations<sup>45</sup>. These reforms need to be ‘situated in a broader agenda of public sector reform’<sup>46</sup> meaning a general overhaul of the legal environment of the respective reforms. However, it is important to note that ‘sound mechanisms of enforcement and supervision both judicial and administrative is often more difficult than the reform of the substantive rules’<sup>47</sup> of the financial services sector in developing countries. Nonetheless, proper sequencing of legal reforms is significant for the success of liberalisation. Consequently, reforms of financial markets would apply to

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<sup>42</sup> *ibid* 417-418.

<sup>43</sup> Florencio López-de-Silanes, ‘The Politics of Legal Reform’, (2002), UNCTAD G-24 Discussion Paper UNCTAD/GDS/MDPB/G24/17, 8

<<http://www.unctad.org/en/docs/pogdsmdpbg24d17.en.pdf>> accessed on 22<sup>nd</sup> April 2011.

<sup>44</sup> Davis K E, and Treblicock M J, ‘Legal Reforms and Development’ (2001) 22 TWQ21.

<sup>45</sup> *ibid* 33.

<sup>46</sup> *ibid*.

<sup>47</sup> *ibid* 4.

substantive and procedural law together with effective enforcement mechanism.<sup>48</sup>  
This must be ‘accompanied by adequate regulation and prudential supervision’<sup>49</sup>.

The legal form and substance of financial regulation and supervision is to a large extent dependent on the factual situation of the market’ therefore ‘form follows function’<sup>50</sup>. Similarly, most financial markets are ‘not exclusively domestic financial markets, but inherently and comprehensively global financial markets’ and their regulation must have a ‘global functional approach’<sup>51</sup>. This underscores the need for NII regulatory framework to have a global outlook through liberalisation.

Insurance reforms and liberalisation facilitates the entry of new domestic and foreign participants through establishment or cross-border activities that ‘could induce a more effective working of the mutualisation and risk spreading process’ and ‘increased capacity to underwrite local risk’<sup>52</sup>. The strengthening of regulatory and supervisory framework alongside slow but cautious liberalisation also helps improve on the efficiency levels of the insurance sector<sup>53</sup>. Consequently, insurance sector liberalisation requires regulatory and supervisory reforms and the liberalisation of the NII would require reforms both in the substantive laws and the supervisory and administrative processes too.

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<sup>48</sup> Lastra (n41) 416.

<sup>49</sup> *ibid*; hence the review of both legislative and institutional provisions in chapters five and six.

<sup>50</sup> Christian Tietje and Matthias Lehmann, ‘The Role and Prospects of International Law in Financial Regulation and Supervision’ (2010) 13 *JIEL* 6.

<sup>51</sup> *ibid*.

<sup>52</sup> UNCTAD, ‘Review of Critical Areas with Regard to Insurance Legislation, Regulation and Supervision, Establishment of effective insurance regulatory and supervisory systems’ (1995) Study by the UNCTAD secretariat, TD/B/CN.4/52, para 10, [http://unctad.org/en/docs/sddins10\\_en.pdf](http://unctad.org/en/docs/sddins10_en.pdf) > accessed 22nd April 2011.

<sup>53</sup> Rahul Sen, and Ramkishan S Rajan, ‘Liberalisation of international trade in financial services in Southeast Asia: Indonesia, Malaysia, Philippines and Thailand’ (2002) 4 *Journal of International Financial Markets* 170,172.

However, it is important that all reforms ‘establish clear institutional benchmarks’ i.e. a standard by which its success or failure can be measured<sup>54</sup>. Therefore, for reforms and liberalisation of insurance, a globally accepted standard or framework would be required. The analysis in the next section focuses on the WTO framework which is the institutional benchmark preferred in this thesis

### **3.1.2 LIBERALISATION IN THE WTO/GATS REGIME**

The WTO is the multilateral trading system created in 1994 to replace the GATT<sup>55</sup> under the Marrakesh Agreement because of the need to enlarge the scope of world trade agreements to accommodate other forms of trade hitherto excluded and alleviate the existing structural problems with the old framework.<sup>56</sup> GATT had for 47 years provided the legal framework for regulating international trade. The WTO authority expanded into new areas with agreements on textiles, agriculture, intellectual property and services while furnishing the legal and institutional infrastructure and the “thickening of legality”<sup>57</sup> of the world trading system. The WTO continued the ‘rules-and-principles-based legal’<sup>58</sup> culture of the GATT while providing ‘the common institutional framework for the conduct of trade relations among its Members’<sup>59</sup> on matters related to the various agreements and

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<sup>54</sup> Thom Ringer, ‘Development, Reform, and the Rule of Law: Some Prescriptions for a Common Understanding of the “Rule of Law” and its Place in Development Theory and Practice’ (2007) 10 *Yale Human Rights and Development Law Journal*, 182.

<sup>55</sup> Rorden Wilkinson, *Multilateralism and The World Trade Organization: The Architecture and Extension of International Trade Regulation* (Routledge, 2000) 11.

<sup>56</sup> This is the agreement establishing the WTO.

<sup>57</sup> David Palmetier, *The WTO as a Legal System*, (Cameron May 2004) 326.

<sup>58</sup> Thomas Cottier and Markus Krajewski, ‘What Role for Non Discrimination and Prudential Standards in International Finance Law’ (2010) 13 *JIEL* 817, 818.

<sup>59</sup> GATS article II.

associated legal instruments included in its annexes. It provides effective facilitation, implementation and administration of these agreements<sup>60</sup> and a forum for negotiations in multilateral trade relations. These agreements are the revised GATT agreement for trade in goods<sup>61</sup>; The General Agreement on Trade in Services (GATS); Trade Related Investment Measures (TRIMS) and Trade Related Intellectual Property Rights (TRIPS) all of which have been ratified in the parliaments of the entire 152 members of WTO including Nigeria<sup>62</sup>.

The WTO functions as an international institution, an agreement, a system of law and a 'linkage machine'<sup>63</sup>. It is 'an integrated, more viable and durable multilateral trading system' for global trade. As an institutional 'forum for international negotiations'<sup>64</sup> and administration of the multilateral trade agreements, the WTO promotes global trade policies which facilitates market access to members and establishes the framework for trade policies by setting the rules<sup>65</sup>.

The WTO successfully links the GATT whose main focus was tariff reductions in goods to other trades such intellectual property and services using the fabric of GATT as foundation of other forms of trade while 'making possible package deals' with issues hitherto unlinked through reciprocity<sup>66</sup>. It therefore consists of the GATT, 'the results of past trade liberalisation efforts' and that of 'the Uruguay

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<sup>60</sup> GATS Article III.

<sup>61</sup> This consist of 'the original GATT, together with its various protocols and decisions, six understandings on interpretation of GATT text, and a 1994 Protocol on tariff concessions; Palmeter (n57) *ibid*.

<sup>62</sup> WTO, 'WTO in Brief' Part 2, <[http://www.wto.org/english/thewto\\_e/whatis\\_e/inbrief\\_e/inbr02\\_e.htm](http://www.wto.org/english/thewto_e/whatis_e/inbrief_e/inbr02_e.htm)> accessed 15<sup>th</sup> December 2005.

<sup>63</sup> Jose E. Alvarez, 'The WTO as Linkage Machine' (2002) 96 AJIL 146.

<sup>64</sup> Agreement Establishing the World Trade Organisation Art III (2).

<sup>65</sup> Hoekman (n39) 41-42.

<sup>66</sup> Alvarez (n63) 147-8.

Round of Multilateral Trade Negotiations'<sup>67</sup>. The WTO has its secretariat in Geneva, Switzerland with over 600 staff headed by a secretary-general which provides technical support for the various councils, committees and the ministerial conferences<sup>68</sup>.

The WTO Agreement has all the elements of a modern system of law<sup>69</sup> and 'one of the most comprehensive collections of primary obligations in the field of public international law'<sup>70</sup> together with secondary rules that are 'presupposed' and 'used'<sup>71</sup>.

The principles and rules of the WTO play a pivotal role in the development of the architecture of the system<sup>72</sup>. Three important aspects of the 'nature of rules'<sup>73</sup> of WTO require adequate consideration for a greater appreciation of this framework. First WTO rules are result oriented rules which do not consider the motive for measures but the impact on trade interests of other members. This means that measures applied in good faith may lead to a breach of obligations under WTO rules. Secondly, these rules provide 'horizontal rights and obligations' between members. Therefore, a breach of obligations by a member automatically attracts rights to seek redress for violation from others. The WTO agreements is thus like a

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<sup>67</sup> Agreement Establishing the World Trade Organisation Preamble.

<sup>68</sup> Sauv  P and Gillespie J, 'Financial Services and The GATS 2000 Round' (2000), Brookings-Wharton Papers on Financial Services, 430 <[http://muse.jhu.edu/journals/brookingswharton\\_papers\\_on\\_financial\\_services/v2000/2000.1sauve.htm](http://muse.jhu.edu/journals/brookingswharton_papers_on_financial_services/v2000/2000.1sauve.htm)> accessed 10<sup>th</sup> April 2011.

<sup>69</sup> *ibid* 312.

<sup>70</sup> Palmeter (n57) 326.

<sup>71</sup> *ibid*.

<sup>72</sup> Cottier and Krajewski (n58) *ibid*.

<sup>73</sup> Claus D. Zimmerman, 'The Neglected Link Between the Legal Nature of the WTO Rules, The Filtering WTO Disputes, and the Absence of Retrospective WTO Remedies' (2012) 4 Trade Law and Development 251, 256.

network of bilateral agreements concluded by all members with each other<sup>74</sup> and a breach of such obligations would be to one or more members who may be affected and entitled to remedies. Furthermore, members' policies are not treated differently whether of international or domestic nature rather, the focus is whether or not it is trade distortive to other members or not. Therefore, the focus of WTO is liberalisation through rounds of negotiations and the principles and rules of WTO are geared towards market opening. The rule based principles at the heart of the WTO framework are Non-Discrimination, Transparency and Reciprocity. However, all WTO principles are considered below i.e. liberalisation and market access, Economic Development, Non-Discrimination, Predictability and transparency, Reciprocity, Fair Competition and Safety Valve.

#### **a. Liberalisation and Market Access**

Liberalisation in the WTO is a principle of market access which involves the lowering of barriers that hamper the free flow of goods and services amongst nations<sup>75</sup>. Liberalisation has been aggressively pursued since the post-World War II reconstructive efforts<sup>76</sup> because free trade is germane for development, world economic stability and general peace. This does not signify trade completely free of barriers but that which continuously lowers barriers. Lowering barriers leads to more open markets and this is achieved through a mechanism for periodic negotiations<sup>77</sup>.

The context of the principle of liberalisation within WTO synchronises with the

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<sup>74</sup> Tarcisio Garzini, 'The Legal Nature of WTO Obligations and Consequences of their Violations' (2006) 17 EJIL 723, 724.

<sup>75</sup> Frank J Garcia, 'Global Justice and the Bretton Woods Institutions' (2007) 10 JIEL 461, 468.

<sup>76</sup> *ibid* 462; Wilkinson (n55).

<sup>77</sup> Wilkinson (n55)20.

theoretical and economic aspects earlier discussed in s3.1 above. Some barriers<sup>78</sup> are nonetheless legal though gradual reduction is sought. The presumption is however that these barriers would eventually go down.

In the same vein, while free trade is pursued for economic growth, evidence shows that sometimes trade openness may fail to bring about growth due to ‘distortions’ in the economy which would require some policies to eradicate<sup>79</sup>. Therefore, countries wishing to liberalise under the WTO/GATS framework need policies in place to address distortions which may hinder growth even with greater openness in trade.

Market access is consonant with the principle of liberalisation by allowing foreign products into the domestic market or domestic goods to penetrate the markets in a foreign country. Market access in WTO involves reciprocated negotiated conditions, tariffs and non-tariff measures agreed between members therefore no general right of market access exists<sup>80</sup>. It is the extent to which foreign goods can compete in a domestic market as negotiated in the WTO by members under different agreements for goods, services and other products with moderations. Domestic and border measures and other forms of restrictions which have distortive effects on trade<sup>81</sup> determine degree of market access and liberalisation in any jurisdiction.

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<sup>78</sup> Such as the exemptions to MFN and allowing PTAs and other existing member agreements under GATS; see discussion s3.2.2 (a).

<sup>79</sup> Somesh K Mathur, ‘Multilateral Trading System and Developing Countries: Prospects and Perspectives with Special Reference to India’ (2002) *Jamia Millia Islamia* 16 <<http://www.cid.harvard.edu/cidtrade/Papers/mathur.pdf>> accessed 23<sup>rd</sup> April 2011.

<sup>80</sup> Harold D Skipper, ‘Insurance in the General Agreement on Trade in Services’ in Claude E Bartfield (ed) *AEI Studies on Services Trade Negotiations* (AEI 2001) 30.

<sup>81</sup> WTO, ‘Services’ (undated) 97 <[http://www.wto.org/english/res\\_e/booksp\\_e/chap4\\_e.pdf](http://www.wto.org/english/res_e/booksp_e/chap4_e.pdf)> accessed 23<sup>rd</sup> April 2011.

In the GATS market access is a negotiable trade obligation in specific sectors and particular mode or modes and this is discussed in detail in Part B of this chapter.

There is an exception to reciprocated market access in the WTO for developing countries under the Special and Differential Treatment<sup>82</sup> (SDT) provisions. This is used to secure the benefit of developed country wealth and resources for the least advantaged states through ‘non-reciprocal market accesses’<sup>83</sup> not linked to liberalisation.

Out of the five notable forms of SDTs<sup>84</sup> in WTO agreements only three are enforceable while the most important ones relating to increasing trade opportunities and safeguarding of the interest of developing countries are either at the discretion of individual developed nations or found to be unenforceable from case law<sup>85</sup>. The enforceable SDTs are those relating to transitional time periods, technical assistance and permitting developing countries to assume lesser obligations. Therefore, the granting of market access is individualized and politicised therefore developed countries use ‘non-trade conditions’ in awarding access which often exclude competitive goods and even services thus offering little or no developmental benefit to LDCs<sup>86</sup>.

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<sup>82</sup> Joel P Tractman and Chantal Thomas (Eds), *Developing Countries in the WTO Legal System* (OUP, 2009) 23, SDTs it exists in various WTO agreements however, GATS Art IV provides for increasing access of LDCs into the markets of developed countries see s3.2.2 (f).

<sup>83</sup> Garcia (n75) 468.

<sup>84</sup> Edwine Kessie, ‘The Legal Status of Special and Differential Treatment Provisions Under the WTO Agreement’ in George A. Bermann and Petros C Maroidis (eds) *WTO Law and Developing Countries* (CUP 2007)

<sup>85</sup> See discussion on increasing participation of developing countries in s3.2.2

<sup>86</sup> *ibid* 469.

These account for disagreements between developed and developing countries on the nature of SDTs though attempts are being made in the current negotiation in Doha to make SDTs ‘more precise, effective and operational’<sup>87</sup>.

## **b. Economic Development**

The WTO promotes economic development and greater flexibility for developing countries to meet obligations as evidenced in its preamble. Economic development means improved life and general well-being of people socially, economically, politically and in all areas of life. The platform provided by the framework for economic development for developing countries are through negotiations and binding commitments or through SDTs discussed above. This became necessary because over 75% of WTO members are either in developing or least developed group of nations. Generally, developing countries are encouraged to embark on legal and trade policy reforms to be able to engage in binding commitments under the framework. The preamble recognises that developing countries need to ‘secure a share in the growth in international trade that is commensurate with the needs of their economic development’<sup>88</sup> but nevertheless desires the ‘entering into reciprocal and mutually advantageous arrangement’ to further these objectives. This means that reciprocal exchange of commitment is the main platform for economic development though, attempts are made at special provisions for LDCs.

The success of SDTs under WTO as earlier noted is questionable since most developing countries are yet to benefit from them in almost two decades of this multilateral trading system. The SDTs have not delivered on economic

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<sup>87</sup> Doha declarations para 44.

<sup>88</sup> Preamble to WTO Agreement.

development<sup>89</sup> because of the application of socio-political rather than economic indices by developed countries. The fact is that the development and determination of the financial and trade needs of developing countries are not well defined in the WTO framework<sup>90</sup>. In consequence therefore, liberalisation and reciprocal commitments appears to be the viable options for the pursuit of economic growth under the framework rather than SDTs.

Nonetheless, Trade Related Technical Assistance (TRTA)<sup>91</sup> coordinated by Institute of Training and Technical Cooperation (ITTC) within the WTO is the most commendable aspect of economic development program for LDCs. This facilitates effective and beneficial participation for developing countries under this liberalising model through training and cooperation aimed at identifying areas of interest for beneficial negotiations.

### **c. Non Discrimination Principles**

This is one of the ‘main instruments of international economic law designed to secure trade liberalisation and guarantee trade commitments’<sup>92</sup>, preventing discriminatory protection of domestic industry or trading partners while averting inefficiencies and market distortions<sup>93</sup>. It emphasises what members should not do with regards to their exercise of regulatory authority<sup>94</sup>. As an instrument of trade

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<sup>89</sup> Tractman and Thomas (n82) *ibid*.

<sup>90</sup> Priscilla Schwartz, ‘Development in World Trade Law’ (2009) 4 *Journal of International Commercial Law and Technology* 50, 54.

<sup>91</sup> See discussion on technical cooperation in s3.2.2 (h).

<sup>92</sup> Nicholas F. Diebold, ‘*Non-Discrimination in International Trade: Likeness in WTO/GATS*’ (CUP, 2010) 17.

<sup>93</sup> *ibid*.

<sup>94</sup> Ortino F, ‘From ‘Non-Discrimination’ to ‘Reasonableness’: A Paradigm Shift in International Economic Law?’ (2005), The European Union Jean Monnet Programme, WP 01/05, 6 <[http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=922524](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=922524)> accessed on 18<sup>th</sup> April 2011.

liberalisation<sup>95</sup> non-discrimination has become central to all global trade arrangements<sup>96</sup> concretized by the mechanisms of Most Favoured Nation (MFN) and National Treatment (NT) Rules which bring level playing fields between foreign and domestic competitors<sup>97</sup>. Non-discrimination has three legal elements<sup>98</sup> first two of which are comparative and principal. These are 'less favourable treatment' and 'likeness' while the third is 'regulatory purpose'. These elements are discussed in detail in Part B.

### **i. Most Favoured Nation Rule (MFN)<sup>99</sup>:**

The MFN rule in WTO like in other 'international economic agreements' embodies the principle of Non-Discrimination by obligating countries to grant every other country with which it has signed a MFN treaty the most favourable treatment it grants to any other country. It prohibits discrimination between foreign suppliers basically on the basis of source of origin<sup>100</sup> or nationality<sup>101</sup>. In the liberalisation framework of the WTO, all advantages and favours granted to a country by one of the contracting parties in respect of a product shall be accorded all other contracting parties. It is one of the pillars of this platform<sup>102</sup> which 'assures equal treatment of products from different countries'<sup>103</sup>. The WTO

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<sup>95</sup> Cottier and Krajewski (n58) 823.

<sup>96</sup> Robert Stern, 'The Multilateral Trading System' (2007) The University of Michigan research Seminar in International Economics Discussion Paper 569, 4  
<<http://www.fordschool.umich.edu/rsie/workingpapers/Papers551-575/r569.pdf>> accessed 23<sup>rd</sup> April 2011.

<sup>97</sup> Cottier and Krajewski (n58) *ibid*.

<sup>98</sup> Diebold (n92) 32.

<sup>99</sup> The GATT Art 1.1; entrenched since the GATT 1947 agreement and inherited by GATT 1994.

<sup>100</sup> Appellate Body Report *European Communities - Regime for the Importation, Sale and Distribution of Bananas (EC – Bananas III)*, WT/DS27/AB/R, adopted 25 September 1997, para 190.

<sup>101</sup> Prabhash Ranjan, 'Bilateralism, MTN and TRIPS : Exploring Possibilities of Alternative Interpretation' (2007) 13 *Int. T.L.R.* 67, 67.

<sup>102</sup> Appellate Body Report in *Canada - Certain Measures Affecting the Automotive Industry*, WT/DS139-142/AB/R (31 May 2000) para 69.

<sup>103</sup> Thomas Cottier, 'From Progressive Liberalization to Progressive Regulation in WTO Law' (2006) 9 *JIEL* 779, 795.

Appellate Body in *US-Section 211 Appropriations Act* dispute reiterated the fact that MFN is ‘central’, ‘essential’<sup>104</sup> and ‘the cornerstone of the world trading system’<sup>105</sup>.

MFN ensures efficient allocation of resources by reducing transaction costs of negotiations for other countries though it encourages ‘free rider countries’<sup>106</sup>. Nevertheless, MFN undeniably promotes liberalisation and it is the essential corner stone of the world trading system without it, the lowering of trade barriers may be impossible because discriminatory trade policies will hamper trade liberalisation. However, this principle is moderated in some WTO agreements such as in the GATS<sup>107</sup> as discussed later in Part B<sup>108</sup>.

## **ii. National Treatment (NT)**

This is the second non-discrimination principle of customary international law which requires that foreign and local products are treated equally. This principle was incorporated by reference in GATT<sup>109</sup> and also in other agreements under the Marrakesh Agreement like GATS. It applies to foreign goods once in the territories of a member country. In the WTO liberalisation framework however, it is an undertaking by ‘members not to use internal policy measures in a

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<sup>104</sup> Chios Carmody, ‘WTO obligations as collective’ (2006) 17 EJIL 419, 425

<sup>105</sup> Appellate Body Report *United States - Section 211 Appropriations Act*, WT/DS176/AB/R (2 Jan 2002), at para 297.

<sup>106</sup> Alice Landau, *The International Trading System* (Routledge, 2005) 10; countries who benefit automatically from concessions they are not a party to.

<sup>107</sup> GATS Art II.

<sup>108</sup> See discussion in s3.2.1 (a).

<sup>109</sup> The GATT Agreement (1994) Art III.

protectionist fashion<sup>110</sup>. This point was affirmed in the WTO *Japan-Alcohol* case where the WTO Appellate Body with reference to earlier cases stated that

*‘Article III obliges Members of the WTO to provide equality of competitive conditions for imported products in relation to domestic products. “[T]he intention of the drafters of the Agreement was clearly to treat the imported products in the same way as the like domestic products once they had been cleared through customs. Otherwise indirect protection could be given”<sup>111</sup>.*

The body further noted that the ‘broad purpose’ of the NT provision was ‘avoiding protectionism’<sup>112</sup>. Therefore, countries with internal measures that afford any form of protection for like domestic products or producers definitely undermine the NT provisions in WTO. Such measures could include taxes, laws, internal charges or any form of regulation that affects sale, purchase distribution or transportation of a product which could be a service or item of intellectual property that has entered the market. WTO members are by this principle obliged to allow fair competition between like domestic products and imported products that are competing with, or substitutes of each other. This is one of the parameters by which a liberalised market is judged. NT does not prohibit the use of internal measures to pursue country economic policies but must ensure that such policies apply equally to all products whether local or imported.

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<sup>110</sup> *ibid*; the article provides that internal taxes, charges and laws affect sale and distribution of goods and should not be applied in a way that it ‘*affords protection to domestic production*’.

<sup>111</sup> Appellate Body Report on *Japan-Taxes on Alcoholic Beverages*, AB-1996-2, WT/DS11/AB/R, 16.

<sup>112</sup> *ibid* 16.

In conclusion, NT generally complements the MFN rule under the non-discriminatory principle. While MFN deals mainly with border discriminatory measures, NT deals with post border internal discriminatory measures and other policies that may indirectly have such consequences. MFN prohibits discrimination between two foreign providers while NT extends the non-discrimination principle to between foreign and domestic producers. The non-discriminatory principles of MFN and NT apply differently in the GATS. For trade in services, NT is not a general principle but a negotiable trade obligation which does not work together with MFN like in other agreements. While the MFN affects the negative-list, i.e. all services not listed in the schedule, the NT affects the positive-list i.e. all services in the schedule of commitments<sup>113</sup>.

#### **d. Predictability and Transparency**

WTO members liberalise and open up their markets under multilateral arrangements by taking up obligations<sup>114</sup> which consists of MFN and NT treatment together with binding commitments. These are guarantees against increase in restrictions on access to markets for trading partners and that no arbitrary charges would be made on goods from producers from trading partners. WTO Members use bindings to convince trading partners, 'business community, domestic and foreign alike, of the stability and predictability of its trading regime'<sup>115</sup>. Hence, 'refusal to bind casts doubt as to the intentions of policy makers to maintain trade liberalisation'<sup>116</sup>. Therefore bindings are essential to liberalisation and free trade so

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<sup>113</sup> See discussion on specific commitments s3.2.2 (a).

<sup>114</sup> See GATT Articles I, II and III; Kyle Bagwell and Robert W Staiger, 'Economic Theory and the Interpretation of GATT/WTO' (2003) 16<

<<http://www.stanford.edu/~rstaiger/econ.theory.gatt.wto.pdf>> accessed 4th April 2011.

<sup>115</sup> Choi Byung-il, 'Treatment of Autonomous Liberalization in the WTO New Service Round' (2001) 35 *JWT* 363, 371.

<sup>116</sup> Mathur (n79) 46.

much that when internal measures such as tariffs, quota or quantitative restrictions increase, guarantees and commitments are undermined.

Trade restrictions negate the aims and functions of the WTO thus, members are mandated to negotiate with their trading partners and if possible consider compensation when changing bindings<sup>117</sup>. A legal obligation accrues to the member to enter into consultations with partners and offer compensation which may be negotiated on another product entirely and not the one in question<sup>118</sup>. Such members are required to consult suppliers, countries of suppliers and then work out modalities for compensation and not go off its commitments abruptly because trading partners are bound to be affected.

Stability and predictability in world trade encourages an objective assumption that binding commitments would not be changed arbitrarily and this motivates other members into altering their resource allocation to increase the production of a particular product based on this commitment. It therefore becomes necessary that compensation would be required to offset trading partners' cost resulting from the member's actions that are contrary to such commitments. Where this fails or is inadequate, retaliatory actions by affected members are also allowed. The Understanding on Rules and Procedures Governing the Settlement of Disputes provides for the withdrawal of concession or obligations 'equivalent to the level of nullification or impairment'<sup>119</sup>.

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<sup>117</sup> GATT Art XIX.

<sup>118</sup> *ibid* Art XXVIII.

<sup>119</sup> WTO Understanding on Rules and Procedures Governing the Settlement of Disputes Article 22.4.

Predictability through binding commitments is of equal significance in trade in services as evidenced in GATS<sup>120</sup> provisions on domestic regulations which require laws to be administered in a consistent and predictable manner<sup>121</sup>. Similarly, the Insurance Model and Best Practices adopted this principle to ensure ‘greater specificity and predictability to those commitments that are important to the industry’<sup>122</sup>. This simply accentuates the significance of predictability to the liberalising model of the WTO/GATS framework to the insurance industry.

Transparency literally means state of being ‘easy to perceive’, or ‘open to public scrutiny’<sup>123</sup>. The principle of transparency requires that information on laws, regulations and its administration and procedures to be readily provided and available to interested parties<sup>124</sup>. This along with non-discrimination principles are fundamental principles of the WTO regime and it requires a ‘bottom-up transparency’<sup>125</sup> to foster fair competition in trade and make information available to both domestic and foreign competitors rather than to ‘a few domestic special interest groups’<sup>126</sup>. Transparency avails other WTO members the opportunity of going through published laws and amendments to laws and regulations of trading partners in order to ascertain its compliance with the WTO framework. The Trade

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<sup>120</sup> See general discussion of GATS in s3.2.2.

<sup>121</sup> The General Agreement on Trade in Services Art VI; Panagiotis Delimatsis, ‘Due Process and "Good" Regulation Embedded in the GATS – Disciplining Regulatory Behaviour in Services through Article VI of the GATS’ (2007) 10 JIEL 13, 28.

<sup>122</sup> See discussion in Chapter Four; John Cooke, ‘Domestic Regulation and Insurance: The Case For a GATS Reference Paper for The Insurance Sector’ (2004) 29 GPRI 284, 293.

<sup>123</sup> Oxford English Dictionary Online, <http://oxforddictionaries.com/definition/english/transparent?q=Transparent> accessed 1<sup>st</sup> July 2012.

<sup>124</sup> Panagiotis Delimatsis, *International Trade In Services and Domestic Regulations: Necessity, Transparency and Regulatory Diversity* (OUP, 2007) 255. GATT Art X though titled ‘Publication and Administration of Trade Regulations’ its provisions are similar to GATS Art II provisions on transparency.

<sup>125</sup> *ibid* (n124) 259; This requires members to send necessary information to the WTO rather than the WTO surveying members policies as it is done in top-down transparency.

<sup>126</sup> *ibid* 256.

Policy Review Mechanism (TPRM) in WTO is charged with the duty of evaluating the extent of transparency in trade rules and practices of member countries.

Though there are extra transparency provisions in the GATS for trade in services as discussed below<sup>127</sup>, transparency generally is significant in the WTO because it promotes rules-based approach of the framework, it provides information to other members and interested parties about the opportunities available in other markets, it facilitates the surveillance on level of compliance to members' WTO obligations and future multilateral negotiations and liberalisations<sup>128</sup>.

As a regulatory principle from the WTO framework transparency is also significant for regulatory reforms and policymaking process in domestic regulations. Regulatory transparency protects regulators from regulatory capture and improves both public confidence in government and investors' confidence in the domestic market<sup>129</sup>. It also helps improve on governance<sup>130</sup>, eradicate systemic deficiencies and discriminatory elements in the regulatory process. Consequently, predictability and transparency both provide guarantees to members about the credibility and trustworthiness of the commitments and regulations of other members. Therefore, these principles would be of benefit to developing countries seeking liberalisation and greater commitment in the WTO/GATS because they both are indispensable to successful liberalisation and regulatory reforms.

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<sup>127</sup> See discussion in s3.2.2 (b).

<sup>128</sup> Delimatsis 'International Trade in Services' (n124) 261.

<sup>129</sup> *ibid* 256-7.

<sup>130</sup> Christine Kaufmann and Rolf H. Weber 'The Role of Transparency in Financial Regulation' (2010) 13 JIEL 779

### e. Reciprocity

WTO encourages reciprocated concessions through negotiations in a give and take process. This is the whole essence of liberalising under a multilateral trading system unlike the unilateral or autonomous liberalisation that attracts no market access into other economies. Reciprocity is paramount in WTO because it ensures gains from liberalisation and limits the free-riding that MFN affords. Non-committing members of WTO enjoy no concession from other members and this has affected most LDCs. What then is the objective of LDCs membership of WTO when they do not engage in reciprocated concessions through commitments?

The limitations to reciprocity lie in the asymmetry of interests of developing and developed nations coupled with the inability of the former to provide adequate regulatory infrastructures for competition<sup>131</sup>. This makes regulatory reforms mandatory for LDCs in order to benefit from reciprocated concessions and market access in the WTO framework for economic development and liberalisation. The likelihood of gaining access or concession without reciprocity is very slim even with the system of preferences and SDTs in place. The negotiations in the Doha round reveal that this asymmetry still subsists even in determining which countries should benefit from SDTs. Significantly, the insistence of developed countries on a graduation provision for developing countries so that none enjoys the SDTs forever is another thorny issue in the current negotiations.

Following the arguments in this thesis, and in line with the postulations of

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<sup>131</sup> Bernard Hoekman, 'The GATS and Developing Countries' in Trachtman and Thomas (n89) 443-445.

Hudec<sup>132</sup>, it would be more beneficial for developing countries to engage in beneficial negotiated and reciprocated market access with technical assistance than rely on SDTs which are mainly unenforceable.

#### **f. Fair Competition**

This complements the non-discrimination principles by ensuring that members' economic policy measures are fair to other trading partners. For instance, anti-dumping rules of the WTO consider it unfair for a country to export goods below cost price just to gain market share in another country. Similarly, where a country takes emergency measures to prevent imported goods from strangling out domestic producers, the WTO assesses its fairness. This ensures that measures are commensurate with the problems to be solved and that consideration is given to non-discrimination principles. Like domestic law, equity must prevail in international trade transactions.

Therefore, as a liberalisation model, the WTO/GATS emphasises the necessity of domestic regulations to offer fair competition which is the only means by which public interest could be served and solvent market is ensured in the insurance sector as noted in chapter two<sup>133</sup>. Fair competition is therefore a principle which would assist in the effectiveness of reforms for growth.

#### **g. Safety Valve**

The principle of safety valve embodies the principle of fair competition and also the use of trade measures in attaining non-economic objectives and the intervention in trade for economic objectives. Sometimes socio-economic

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<sup>132</sup> Robert Hudec, *Developing Countries in the GATT Legal System* (Gower, 1987) 159-160

<sup>133</sup> See s2.4.

conditions are injured by competition and liberalisation protection consequently, the WTO allows members use measures for non-economic objectives and protective policies on national security or public health or domestic industries just to enable domestic market adjust. Measures are also allowed to correct balance of payment problems or a country's desire to protect its infant industry<sup>134</sup>. The impression is created that the safety valve principle is contrary to the liberalisation framework of the WTO because of its continuous abuse by developing countries without recourse to WTO requirements. It is actually geared towards the achievement of objectives of WTO such as improved living standards and economic development.

When using the WTO/GATS as a liberalising model, it is pertinent to note that conflicts may arise in the application of the WTO safety valve provisions together with conditions of other developmental organizations like IMF or even other agreements such as GATS. In the *India-Balance of Payments Case*<sup>135</sup> the decision of the panel were based on the opinion of IMF. Similarly, the adoption of capital controls to address a financial crisis for socio economic reasons allowed under WTO general obligations is a violation under the GATS. This implies that the application of caution would be necessary for developing countries that may wish to use this safety measures in order to avoid actions from other members.

The above analysis has shown that the WTO helps trade flow smoothly, freely,

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<sup>134</sup> Art. XII and XVIII: B of GATT 1994; The Understanding on the Balance-of-Payment Provisions of GATT 1994 and Art. XII of GATS. Developing countries are also allowed flexibility in the use of quantitative restrictions for balance of payment reasons in Art XVII:2 (b).

<sup>135</sup> Appellate Body Report in *India- Quantitative Restrictions on Imports of Agricultural, Textile and Industrial Products*, AB-99-3, WT/DS90/AB/R where a decision of IMF was the basis for striking out India's appeal against panel ruling.

fairly and predictably through the administering of the trade agreements, while acting as a forum for trade negotiations, settling trade disputes and reviewing national trade policies. The principles supports liberalisation and the necessary reforms needed to facilitate it. WTO encourages the greater participation of the majority of its members and consequently increases world trade through the dismantling of trade barriers. It not only provides for an institutional framework for the conduct of trade in goods and services and other forms of trade provided in the agreement but also facilitates trade. The Agreement and its annexes, also enable countries to come together to exchange market access commitments on reciprocal basis<sup>136</sup>.

WTO also uses special assistance mechanism to facilitate liberalisation in developing countries. This is coupled with the activities of the Committee on Trade and Development which reviews periodically the special provisions in the agreement in favour of LDCs and reports to the General Council. Disappointingly, large number of LDCS have neither embraced these mechanisms for assistance nor participated actively in the WTO. This is due to perceptions that the processes and mechanisms of the WTO are weighted against them and their 'inherent inadequacies'<sup>137</sup>.

Consequently, the Doha Round agenda has specifically devoted some time to discussing how to help developing countries in the WTO achieve higher levels of

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<sup>136</sup> Hoekman (n39) 41-2.

<sup>137</sup> Richard Blackhurst, Bill Lyakurwa and Ademola Oyejide, 'Options for Improving Africa's Participation in the WTO' (2000) 23 World Economy 491, 494-5; These are inadequate capacities to monitor trade policies of key trading partners and 'limited personnel with requisite knowledge of international trade law'. This is further compounded by problems of poor capacity to articulate, coordinate and implement trade policy at national level.

development through trade liberalisation and greater participation within the framework. The non-obligatory nature of the provisions for assistance and development of developing countries seems to amplify the belief that WTO is largely based on the western agenda to gain access to markets of developing countries. It is pertinent to ask whether developing countries stand a better chance in terms of economic development outside WTO such as in regional or bilateral arrangements. Similarly, how effective can the clamour for special and differential treatment be in a principle and a rule based framework?

This thesis argues that it would be more favourable for developing countries to liberalise, engage in strategic negotiations and binding commitments as opposed to agitating for special treatment which is neither enforceable nor certain and which has often not delivered<sup>138</sup>.

The GATS model of insurance liberalisation being proposed for the liberalisation of the NII is the ‘first ever set of multilateral legally binding rules covering international trade in services’<sup>139</sup> and the framework commonly used for service liberalisation globally. The GATS is the effective framework under which most liberalisation of insurance has occurred in the last sixteen (16) years. This is because it allows regulatory autonomy and progressive liberalisation in services for its member countries. Thus the second part of this chapter would discuss the general framework of the GATS.

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<sup>138</sup> See discussion on technical cooperation in s3.2.2.

<sup>139</sup> Skipper (n80) 26.

## PART B

### 3.2 GATS GENERAL FRAMEWORK FOR LIBERALISATION

International trade in services used to be regarded as impossible in pre-WTO years because domestic regulations of most countries prohibited it<sup>140</sup>. GATS was the agreement that broke ‘new grounds’ when it came into effect on the 1<sup>st</sup> of January 1995 as part of the Marrakesh Agreement<sup>141</sup>. The forcing of services on the agenda for discussion during the Uruguay Rounds<sup>142</sup> marked the beginning of a new agenda in the world trade liberalisation negotiation serving as a ‘monument to the proposition that services can be subject to international trade rules akin to those for goods’, and that the inclusion of services is essential in world economy<sup>143</sup>.

GATS is contained in Annex 1 of the *Marrakesh* Agreement and it is the first set of multilateral legally binding rules covering international trade in services. It is a legal framework that has been effectively used as a benchmark for liberalisation efforts in a lot of countries<sup>144</sup>. GATS provides the ‘multilateral legal framework for

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<sup>140</sup> Ronald W Jones, and Frances Ruane, ‘Appraising The Options in International Trade in Services’ (1990) 42 Oxford Economic Paper 672.

<sup>141</sup> Eric H Leroux, ‘Eleven Years of GATS Case law: What have we learned?’ (2007) 10 JIEL 749, 751.

<sup>142</sup> Jane Kelsey, *Serving Whose Interest: The Political Economy of Trade in Services Agreement* (Routledge-Cavendish, 2008) 58; S P Shukla, ‘From GATT to WTO and Beyond’ (2000) UNU/WIDER WP No. 195, 14.

<sup>143</sup> Skipper(n80) 1.

<sup>144</sup> China, Wei Zheng, ‘China’s Insurance Industry: Reform, Opening and Development’, in *Trade and Development Aspects of Insurance Services and Regulatory Framework* UNCTAD/DITC/TNCD/2007/4, 153-198  
<[http://www.unctad.org/en/docs/ditctnkd20074\\_en.pdf](http://www.unctad.org/en/docs/ditctnkd20074_en.pdf)> accessed 23<sup>rd</sup> April 2011; South Africa; James Hodge, ‘Examining the Cost of Services Protection in a Developing Country: The Case of South Africa’ (World Services Congress, Atlanta, November, 1999); India; Tony Singh Anuroop,, ‘Benefits of Insurance Liberalization in India: A Case Study’, in *Trade and Development Aspects of Insurance Services and Regulatory Framework* (2007) UNCTAD/DITC/TNCD/2007/4, 243-7; Aaditya Mattoo, R Rathindra and A Subramanian, ‘Measuring Services Trade Liberalisation and its Impact on Economic Growth: An Illustration’ (2001) World Bank Policy Research WP 2655, <<http://elibrary.worldbank.org/docserver/download/2655.pdf?expires=1303562687&id=id&accna me=guest&checksum=F647C4AF5823B29D266EB8542EEC8605>> accessed 23<sup>rd</sup> April 2011

over 95 percent of world trade in financial services'<sup>145</sup>, which implies that to be relevant in trade in services, the Nigeria needs to be liberalised its insurance services under this framework.

The GATS is largely administered under WTO like other agreements but some provisions of the GATS make it deviate from other agreements in some key areas which would be discussed below<sup>146</sup>. The GATS framework allow a considerable amount of flexibility by ensuring that countries can progressively liberalize their economy at a convenient rate in consideration of each country's economic situation. Therefore, the attractive characteristics of GATS for developing countries mainly are flexibility and progressiveness. The GATS presents a framework for countries to progressively liberalize their economy at a rate that will favour the realities of their individual economies in sectors they are comfortable in.

The advantage which GATS has over other framework for liberalisation of services and insurance include the fact that it is also principles and rule based; it allows members supplement domestic reforms for growth and development with binding commitments while also operating as a model for the comparison of liberalisation. The GATS also involves an understood system of liberalisation which provides guarantees for service suppliers in other countries about measures

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USAID, 'Assessment on How Strengthening the Insurance Industry in Developing Countries Contributes to Economic Growth' (2006) 10, <[http://pdf.usaid.gov/pdf\\_docs/PNADF482.pdf](http://pdf.usaid.gov/pdf_docs/PNADF482.pdf)> accessed 12<sup>th</sup> August 2011.

<sup>145</sup> Skipper (n80)1.

<sup>146</sup> *Canada-Certain Measures Concerning Periodicals*, WT/DS31/R, 69-70; it was stated that GATT and GATS are not mutually exclusive though they often overlap; Eric H Leroux, 'Eleven Years of GATS Case law: What have we learned?' (2007) 10 JIEL 749, 750-2.

in committed sectors<sup>147</sup>.

GATS operates at three levels namely framework agreement which sets out general principles of GATS; the annexes containing rules for specific services sectors such as finance (insurance and banking) and telecommunications and the Schedules listing the commitments and exemptions of each signatory country.

The Agreement contains twenty nine (29) articles broken down into six parts; Scope and Definition, General Obligations and Disciplines, Specific Commitments, Progressive Liberalisation, Institutional Provisions and Final Provisions. The last article contains the annexes containing agreements in specific services such Air Transport, Financial Services, Negotiations on Maritime Transport Services and Telecommunications.

The Agreement defines the scope of GATS as applying to ‘measures by members affecting trade in services’<sup>148</sup>. To understand GATS, it is necessary to define some terminologies used in the agreement such as services, sectors, schedules and modes of supply.

### **3.2.1 Definitions**

#### **a. Concept of Services**

Service is not defined in the GATS but enclosed within the concept of trade in

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<sup>147</sup> Association of British Insurers, ‘Liberalisation of Insurance Services in GATS, in Trade Development Aspects of Insurance Services and Regulatory Frameworks, Paper delivered at the UNCTAD Adhoc expert meeting on insurance services held on 24 November 2005 at the Palais Des Nations, Geneva <[http://www.unctad.org/en/docs/ditctncd20074\\_en.pdf](http://www.unctad.org/en/docs/ditctncd20074_en.pdf)> accessed 23<sup>rd</sup> April 2011.

<sup>148</sup> General Agreement on Trade in Services Art 1.

services which is also defined along four modes of supply as discussed below. The Agreement however states that services include ‘any service in any sector except that supplied in the exercise of government authority’<sup>149</sup>. This is defined as services not supplied on a ‘commercial basis’ or in ‘competition with other service suppliers’<sup>150</sup>. For ‘government authority’ the GATS recognises central, regional or local government and even delegated authority to non-governmental organisations. It is pertinent to note that this exception to GATS does not operate like a blanket cover because government services supplied in competition or for profit still falls under the ambit of the GATS. Therefore, despite various contradictory interpretations of ‘the context, object and purpose of the provisions in the GATS’<sup>151</sup>, the nature of the service and the characteristics of the seller are irrelevant in the definition of services. The conditions of competitiveness and profitability are the keys to understanding the nature of services covered under the GATS. Consequently, services can be supplied on commercial basis or in competition with other suppliers whether by private, public or government bodies.

However, conflicts could arise for example where social services are provided by private organizations on behalf of government on part commercial part charity basis. In these circumstances it might be difficult to determine what is excluded from the GATS. More importantly within the purview of this thesis, developing countries usually do not have the resources for providing some social services normally provided by government and often delegate this to private service suppliers. The implication of this is that normal public services like education,

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<sup>149</sup> *ibid* Art 1(3)(a).

<sup>150</sup> *ibid* Art 1 (3)(c).

<sup>151</sup> Markus Krajewski, ‘Public Services and Trade Liberalization: Mapping the Legal Framework’ (2003) 6 *JIEL* 341,353.

water and health services may come under GATS contrary to the aims of this model. Public service is both a constitutional and human right entitlement which government authorities ought to provide their citizens<sup>152</sup>. This has led to the argument that the GATS protects private property rights but fails to do same for public services rights thereby creating a conflict between national regulations and liberalisation<sup>153</sup>. Hence the agitation for a human rights approach to trade law<sup>154</sup>.

However GATS 'Services Sectoral Classification Lists'<sup>155</sup> a flexible but positive indicator<sup>156</sup> of whether an activity belongs to the services sector classified a total of 155 services under twelve groups. The twelfth group is termed 'other services not included elsewhere'. Since this list forms the basis for scheduling specific commitments, the implication is that the open and flexible disposition of the list has created an avenue for further development of service groups in future negotiations.

Nonetheless, insurance and insurance related services come under financial services group on the list along with banking and other related services. Insurance is further broken into four subsectors which are Life, accident and health insurance services; Non-life insurance services; Reinsurance and retrocession and Services

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<sup>152</sup> Markus Krajewski, 'Public interests, private rights and the "constitution" of GATS' ("GATS: Trading Development?" Workshop, Centre for the Study of Globalisation and Regionalisation, University of Warwick 20 and 21 September 2002) 4-6

<sup>153</sup> *ibid* 10.

<sup>154</sup> *ibid* 12; UNESCO, Commission on Human Rights, Sub-Commission on the Promotion and Protection of Human Rights, "Liberalisation of trade In services and human rights", Report of the High Commissioner, 25 June 2002, E/CN.4/Sub.2/2002/9.

<sup>155</sup> Group of Negotiations on Services, Uruguay Round, Services Sectoral Classification List, Note by Secretariat, MTN.GNS/W/120, 10 July 1991.

<sup>156</sup> Diana Zacharias, 'Article I GATS: Scope and Definition' in in Rüdiger Wolfrum, Peter-Tobias Stoll and Clemens Feinäugle (eds) *Max Planck Commentaries on World Trade Law WTO-Trade in Services* (Vol 6 Martinus Nijhoff Publishers 2008) 42.

auxiliary to insurance (including broking and agency services)<sup>157</sup>.

Insurance service is a subsector of the financial services sector and life assurance is a subsector of insurance services. A member could choose to make commitments under the reinsurance sector of insurance and not in any other insurance service or another subsector of maritime transport services. This further reflects the flexibility associated with the GATS and in addition, it is a framework which would be very amenable to developing countries because they can dictate the pace and level of liberalisation of different service sectors and subsectors in the economy.

The Agreement further elaborates on the term ‘service of another member’ and ‘service supplier’<sup>158</sup>. Service of another member are services from or in the other member’s territory, maritime vessels or the person of that other member that supplies with the maritime vessel either in whole or in part. On the other hand, a service supplier is defined as any person supplying the service and this person could be either a natural person or juridical person. Therefore, a service supplier could be either a natural or juridical person. This implies that liberalisation in the GATS includes corporate suppliers of services and professionals that supply services such as claim assessors, fire engineers and average adjusters working in the insurance industry.

Furthermore, services of another member need not be physically from another

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<sup>157</sup> Services Sectoral Classification (n155) Group 7 (A); see s4.1 (a) for detailed discussion on insurance subsectors.

<sup>158</sup> The General Agreement on Trade in Services Art XXVIII (f) & (g).

member but even ships or vessels registered in another member's territory from which service is supplied partly or in whole. This is a very important aspect of international maritime law forming part of GATS provisions because vessels registered in another member's jurisdiction is viewed as an extension of the territory of the member. This aspect of GATS broadens the scope of obligations of members because internal measures need to take cognisance of obligations towards vessels used in supply of services and also corporate and professional suppliers of services of other members in committed sectors. The latter in particular having implications for members' immigration laws and thus require some form of reforms in scheduled commitments.

#### **b. Schedule**

In the WTO, each member has a schedule on which its commitments on various classes of goods and services are listed. Schedules are also an integral aspect of GATS legal instruments indicating the scope of market access and NT commitments of members. Members have a schedule of commitments and exemptions in sectors and the modes covered by the agreement. There is also a schedule of Specific Commitments (Art XX) where members state among other things the terms and conditions for market access and qualifications for NT. This contains undertakings relating to additional commitments, and where appropriate, dates of entry into force and the time frames for implementation. It is important for each member to inscribe in its schedule any measure that is inconsistent with GATS provisions on NT and market access. These schedules are annexed to the GATS Agreement and are not intended to modify general market access and NT provisions in GATS. The Appellate body in the *US Gambling and Betting* noted

that schedules represent ‘a common agreement among all members’<sup>159</sup> and its interpretation is to be made with reference to the Scheduling Guidelines of 1993 and the service sector classification list (W/120 List)<sup>160</sup>. Consequently, members that do not intend to schedule under this guideline and classification need to state so explicitly<sup>161</sup>.

Modification and withdrawal from the commitments on schedule is allowed for members after three years of entry into force of the commitment and at least three months before the proposed date of modification. Members affected by this decision may request negotiation for the purpose of compensation<sup>162</sup>. The Council for Trade in Services establishes the procedures for modification and withdrawal of commitments or schedule<sup>163</sup>.

This is a significant aspect of the GATS model to developing countries because it provides a ‘pull out option’ where commitments are not working in members’ interest. However, this may be a long and costly process requiring compensatory adjustments for all affected members. All the same, it encourages countries to liberalise and enter into binding commitments in more sectors in consideration of the exit options available in the framework.

Fortunately, discussions on emergency safeguard measures are on the agenda in the current round of negotiations in response to developing countries continued

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<sup>159</sup> Appellate Body Report on *US - Measures Affecting the Cross-Border Supply of Gambling and Betting Services*, WT/DS258/AB/R adopted April 2005, para 159.

<sup>160</sup> Services Sectoral Classification (n155).

<sup>161</sup> Krajewski ‘Service Trade Liberalization (n24) 172.

<sup>162</sup> See s3.1.2(d)

<sup>163</sup> The General Agreement on Trade in Services Article XXI.

agitation for clarity especially with regards to modification and withdrawal of commitments.<sup>164</sup> These measures are required for temporary relief or protection from difficulties that could arise as a result of liberalisation commitments and obligations<sup>165</sup> and more importantly to further encourage liberalisation in services. When firm decisions are made on justification, appropriate measures and duration of these safeguards<sup>166</sup> together with other relevant issues, further commitments could be assured.

### **c. Modes of Supplying Services**

This is the most unique feature of the GATS. It is the basis on which commitments and limitations on market access and NT are scheduled. The GATS recognizes four modes by which services could be supplied. Though legally, these modes are interconnected<sup>167</sup>, it is sometimes practically impossible to distinguish these modes in reality due to some identified overlaps in the elements or processes involved some of these modes.

Cross Border supply ‘from the territory of one member into the territory of another member’ involves the supplier remaining in its country of operation and supplying services to consumers in other countries. Both buyer and seller remain in their individual positions. This is often the practice in reinsurance business where insurance companies buy their reinsurance covers from reinsurance firms outside their jurisdictions. UK and Germany have a substantial reinsurance market with

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<sup>164</sup> Rudolf Adlung, ‘Negotiations on Safeguards and Subsidies in Services: A Never-Ending Story?’ (2007) 10 JIEL 235,236.

<sup>165</sup> Wendy Dobson, ‘Financial Services and International Trade Agreements’ in Aaditya Mattoo, Robert M. Stern and Gianni Zanini, (eds) *A Handbook of International Trade in Services* (OUP, 2008) 306.

<sup>166</sup> Krajewski ‘Service Trade Liberalization’ (n24) 170.

<sup>167</sup> Kelsey (n142) 25.

customers from both developed and developing countries.

The second mode is consumption abroad where the consumer moves to the supplier's country to purchase its services. Examples are found in insurance of special classes involving large sums insured such as oil and gas, aviation and marine insurances and sometimes in health insurance where the insured may need to purchase cover outside its country where expertise and capacity exist for such classes. An interesting overlap could exist in the purchase of health insurance policies which may technically involve elements of both cross border supply and consumption abroad element. The service may be bought in a particular jurisdiction but parts of the benefits are available in jurisdictions where the service provider is not resident e.g. in cases of emergency airlifting of consumer from country of residence to country of service provider. It is important to note however that consumption abroad mode of supply usually is outside the control of countries because people are free to move in and out of the country so long as they have the required documents to do so. However, regulations can be put in place putting such transactions under the ambit of the law.

Commercial presence is the third mode of supply and this involves foreign suppliers maintaining local presence in another country. Here, the foreign service-provider actually establishes its presence by fulfilling the necessary conditions of its host country through a branch, joint venture, franchise or licensing. There are a lot of insurance companies setting up operations outside their country of registration. Similarly, many UK registered insurance companies used to exist in this form in Nigeria in the 1950's and 1960's before the indigenisation

programmes of the 70s<sup>168</sup>. However, currently the world biggest insurance companies like AXA, AIG, Allianz from UK and US all have presence many countries outside their home country.

The last mode of supply is the temporary movement of natural persons in the territory of any other members. It often involves professionals going to the host country for the purpose of offering particular services. In insurance services this includes movement of international loss adjusters from European countries or US for the purpose of adjusting claims in highly specialised classes of insurance. This reinforces the need for the liberalisations of insurance because professional service-providers need to be able provide their services without restrictions.

These modes of supply have become ‘canonical’ in the definition of trade in services<sup>169</sup> both in academic analysis, trade policy-making and trade agreements on services<sup>170</sup>. Therefore as a model for regulatory reforms, the definition of trade in services in GATS would help structure the trade policy of Nigeria in insurance and restructure the domestic regulations in a way to reflect the various modes of trade ensuring adequate regulatory provisions are made for each mode bearing in mind the various effects each would have on the domestic situation of the NII.

#### **d. Measures affecting trade in services**

The GATS ‘applies to measures by Members affecting trade in services’<sup>171</sup>.

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<sup>168</sup> The Nigerian Enterprises Promotion Decree of 1972 set out to make Nigeria economically But has been criticised as having sacrificed economic efficiency in the drive to replace foreign nationals with Nigerians; Chibuzo S A Ogbuagu, ‘The Nigerian Indigenisation Policy: Nationalism or Pragmatism?’ (1983) 82 *African Affairs* 241.

<sup>169</sup> Andrew Lang, ‘GATS’ in Bethlehem et al. (eds.), *The Oxford Handbook on International Trade Law* (OUP, 2009) 157, 161.

<sup>170</sup> Krajewski ‘Service Trade Liberalization’ (n24) 160.

<sup>171</sup> General Agreement on Trade in Services Art1 (1).

Applying the definition of ‘measure’ in Article XXVIII of the agreement, measures affecting trade in services encompasses any form of regulation, law, rule, procedure or administrative decision which may affect the purchase, use, payment, access or connection to a service being offered to the public.

However from WTO jurisprudence, the definition of measures affecting trade had been addressed in the *EC – Banana III*<sup>172</sup> where the Appellate Body stated that,

*“the use of the term "affecting" reflects the intent of the drafters to give a broad reach to the GATS. The ordinary meaning of the word "affecting" implies a measure that has "an effect on", which indicates a broad scope of application”*

Therefore, measures refer to all actions and exclude none *a priori* for as long as it affects the ‘production, distribution, marketing, sale and delivery of a service’<sup>173</sup>. In essence, any action whether legal or administrative that can hamper the free sale and purchase of a service is a measure affecting trade in services. Once a member makes commitments under the GATS, it is bound to ensure that its measures are compliant with GATS obligations to the extent of the limitations on its schedule. The Appellate Body in the above case in identifying the three categories of measures also made it clear that:

*“Certain measures could be found to fall exclusively within the scope of the GATT 1994, when they affect trade in goods as goods.*

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<sup>172</sup> Appellate Body Report in *EC – Bananas III* (n100), 220 and Panel Report WT/DS27, para 7302.

<sup>173</sup> *ibid.*

*Certain measures could be found to fall exclusively within the scope of the GATS, when they affect the supply of services as services.*

***There is yet a third category of measures that could be found to fall within the scope of both the GATT 1994 and the GATS<sup>174</sup>. These are measures that involve a service relating to a particular good or a service supplied in conjunction with a particular good. In all such cases in this third category, the measure in question could be scrutinized under both the GATT 1994 and the GATS”.***

The legal effect of this decision is an extension of liability whereby a member of WTO that is also a signatory to GATS may become liable indirectly under GATS for measures it had taken in respect of its obligations under the GATT. This decision has broadened the application of measures affecting trade in services to include both direct and indirect measures for as long as it affects the production, distribution, marketing, sale and delivery of a service. This interpretation was affirmed by the Appellate Body in the *Canada- Auto* where it was stated that the provision reflected the intention of the drafters to give the agreement a broad scope<sup>175</sup>.

It is however pertinent to note that the obligations of members with regards to measures extend beyond central government in the GATS<sup>176</sup>. These include measures taken by ‘regional or local governments and authorities’ and non-governmental bodies exercising powers delegated to them by the government bodies<sup>177</sup>. This as noted by Kelsey may give rise to tensions in ‘sub-national

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<sup>174</sup> Emphasis is mine

<sup>175</sup> Appellate Body Report on *Canada -Automotive Industry* (n102) para. 78, 159.

<sup>176</sup> Kelsey (n142) *ibid.*

<sup>177</sup> Art 3.

powers' in the exercise of either constitutional or statutory authority in federal or unitary states respectively<sup>178</sup> given the fact that GATS obligations bind all levels of government of member states including licensing and professional bodies<sup>179</sup>. However, this tension is mitigated by the fact that only states are required to take 'reasonable measures available' to ensure observance by both governmental and non-governmental bodies though no definition is provided by the GATS of what constitutes 'reasonable measures available'<sup>180</sup>.

The significance of this is that as a liberalizing framework for NII, attention has to be paid to both government and non-government measures on trade in goods as much as that of services. Secondly, Nigeria's adoption of the GATS regulatory model and further commitment in the GATS framework needs to take into consideration both its federal nature and constitutional provisions in this regard. Though insurance falls under the executive lists in the constitution, other non-governmental organisations such as the various bodies and associations take measures which may impact on the obligations of the country in the GATS. Scheduling of commitments would require a careful consideration of all these measures and determination of a reasonable level of liberalisation in the sectors and modes for which market access and NT are to be allowed including appropriate limitations. Once the schedule of commitment is signed, it becomes binding on the country and attempts at introducing new measures would require some administrative processes which require a minimum number of years to revert the obligations under the schedule. Furthermore, countries that have made careless

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<sup>178</sup> Kelsey (n142) *ibid*

<sup>179</sup> *ibid*.

<sup>180</sup> The General Agreement on Trade in Services Art III.

commitments in the GATS have had to face severe consequences as demonstrated by the Appellate Body's decision in *US Gambling* case<sup>181</sup>.

From the above analysis, it is significant to note that unlike in other forms of trade, the regulation of services require carefully drafted laws and an efficient and adequate regulatory body to regulate the activities in the services sector as stressed in chapter two<sup>182</sup>.

### **3.2.2. GATS REGULATORY MODEL FOR LIBERALISATION**

The provisions of GATS have become a model for regulatory reforms and liberalisation in services. It promotes 'greater competition in the market and non-discrimination against foreign services and service suppliers' which leads to a more rational and economic market structure<sup>183</sup>. The regulatory principles of market access and NT among others (especially in Article VI) provide models for an efficient and trade friendly regulatory structure. This model is noted for its efficacy in regulations geared towards market openness<sup>184</sup>. Trade in the GATS is defined along the four modes of supply<sup>185</sup> which represent the main ways in which trade in services can take place. This provides more than one means of encouraging trade in countries wishing to liberalise its service sectors.

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<sup>181</sup> Appellate Report on *US - Gambling* (n159); Krajewski 'Service Trade Liberalisation' (n170) 158.

<sup>182</sup> See s2.4.

<sup>183</sup> Juan Marchetti, 'Developing Countries in the WTO Services Negotiations' (2006) World Trade Organization ERSD Staff WP 2004-06, 82-128

<sup>184</sup> Anthony Kleitz, 'Experience and Best Practices in Achieving Regulatory Efficiency and Open Markets' (OECD Regulatory Management and Reform Seminar, Moscow, 19-20 November 2001) 3.

<sup>185</sup> As analysed above in s3.2.1.

Though the general obligations under GATS are the MFN and transparency<sup>186</sup>, the unique pro-liberalisation principles it provides include the definition of trade, distinction between general obligations and specific commitments (complemented by the Bottom-up Approach), Progressive Liberalisation and Domestic Regulation Requirements, Technical Cooperation and so on. These are principles governments can adopt and adapt to domestic situations in the process of regulatory reforms and liberalisation.

#### **a. Distinguishing GATS General and Specific Liberalisation Commitments**

WTO members generally are obliged to abide by principles of the framework<sup>187</sup> whether committed or not any sector as earlier noted. However, the GATS for the first time in international economic law introduced a system which allows members designate sectors and modes of supply to take on market access and NT obligations<sup>188</sup>, thereby creating specific commitments. A Specific commitment is an ‘undertaking to provide market access and NT for a service ... on the terms and conditions specified in the schedule’<sup>189</sup>. All the general commitments of the WTO also apply to signatories to GATS except for the MFN, transparency and NT principles which apply with degrees of variation in the GATS. The first two are general commitments in GATS and they are set out in Part II of the agreement while specific commitments are contained in Part III<sup>190</sup>.

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<sup>186</sup> Mamiko Yokoi-Arai, ‘GATS’ prudential carve out in financial services and its relation with prudential Regulation’ (2008) 57 ICLQ 613, 619; See discussion on MFN and Transparency principles s3.1.2 (c) and (d).

<sup>187</sup> See discussion on WTO principles above.

<sup>188</sup> See discussion on schedules above in s3.2.1 (b).

<sup>189</sup> WTO, ‘Services: Guide to Reading the GATS schedules of Specific Commitments and the list of Article II (MFN) Exemptions’ <[http://www.wto.org/english/tratop\\_e/serv\\_e/guide1\\_e.htm](http://www.wto.org/english/tratop_e/serv_e/guide1_e.htm)> accessed 22<sup>nd</sup> July 2012.

<sup>190</sup> Note part of Art VI relate to procedural aspects of general obligations.

### *General Commitments*

The general obligations set out in Part II of GATS are MFN, Transparency and other additional duties<sup>191</sup>.

Article II of the GATS contains MFN provisions as follows:

*“With respect to any measure covered by this Agreement, each Member shall accord immediately and unconditionally to services and service suppliers of any other Member treatment no less favourable than that it accords to like services and service suppliers of any other country”*<sup>192</sup>.

Bearing in mind the earlier definition of ‘measure’ and ‘service of any other member’,<sup>193</sup> this implies that all actions by a member with regards to services or service suppliers of other country must apply equally to the service or the service suppliers from the GATS members and also services from or in the other member’s territory, maritime vessels or the person of that other member that supplies with the maritime vessel either in whole or in part. It also includes for commercial presence or natural persons.

The term ‘treatment no less favourable’ was interpreted in the *EC-Banana III* by the WTO Appellate Body to include both ‘*de facto*’ and ‘*de jure*’ i.e. both formal and informal discrimination<sup>194</sup>. According to the body:

*“The obligation imposed by Article II is unqualified. The ordinary*

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<sup>191</sup> Rudolf Adlung and Aaditya Mattoo, ‘The GATS’ in (eds) Aaditya Mattoo, Robert M. Stern and Gianni Zanini) *A Handbook of International Trade in Services* (OUP, 2008) 63

<sup>192</sup> The General Agreement on Trade in Services Art II (1).

<sup>193</sup> See s3.2.1(d)

<sup>194</sup> Appellate Body *EC – Bananas III* (n100) para 234.

*meaning of this provision does not exclude de facto discrimination. Moreover, if Article II was not applicable to de facto discrimination, it would not be difficult -- and, indeed, it would be a good deal easier in the case of trade in services, than in the case of trade in goods -- to devise discriminatory measures aimed at circumventing the basic purpose of that Article*"<sup>195</sup>

De facto discrimination 'does not formally discriminate against foreign services and service providers' but 'has the same or similar effect as a formally discriminating measure'<sup>196</sup>.

Therefore under the liberalisation framework of GATS a member is obliged to avoid formal or informal discrimination to either natural or juridical persons from or in any other member country that provides services in the said member's territory, whether in commercial presence or entry of natural persons mode, when the service is supplied directly or through the operation of a maritime vessel either wholly or in part.

On the other hand, the standard of 'likeness' can be determined using the objective standards, economic standard using competitive relationships<sup>197</sup> or the subjective standard which focuses on the regulatory purpose<sup>198</sup>. However, this thesis aligns

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<sup>195</sup> Ibid para 233.

<sup>196</sup> Krajewski 'National Regulation and Trade Liberalization' (n4)108.

<sup>197</sup> Diebold (n92); Andrew Lang, 'The GATS and Regulatory Autonomy: A Case Study of Social Regulation of the Water Industry' (2004) 7 JIEL 4,822-23;

<sup>198</sup> Diebold (n92) 173, Nicholas Diebold, 'Non-Discrimination and the Pillars of International Economic Law' NYU School of Law IILJ Emerging Scholars Paper 18 (2010)5-8.

with the economic standards approach given the GATS provisions on NT which defines differential treatment on the basis of ‘modification of competitive conditions’<sup>199</sup>. However, the Appellate Body in *EC-Asbestos*<sup>200</sup> had warned that the spectrum for the degree of ‘competitiveness’ and ‘substitutability’ to indicate likeness was ‘difficult if not impossible’<sup>201</sup>.

Nonetheless, MFN principles should apply equally to all service providers from different countries when they compete<sup>202</sup> except in some situations. These includes where it is listed as exemptions on the schedule of commitments, in other instruments of exemptions found under economic integration agreements<sup>203</sup> and recognitions relating to standards, certificates and so on<sup>204</sup>.

Subsection (2) of Article II of GATS provides that:

*“A Member may maintain a measure inconsistent with paragraph 1 provided that such a measure is listed in, and meets the conditions of, the Annex on Article II Exemptions.”*

This provides members with exemptions from MFN obligations in subsection (I) for some specific measures in place at the time of entry into force of the GATS Agreement for a period of not more than Ten (10) years. It is a one-off measure renewable only upon notification of the WTO secretariat. The Council of Trade in Services provides a form of confidence reinforcement through its review and monitoring of listed MFN exemptions by members. This provision ensures there

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<sup>199</sup> General Agreement on Trade in Services Art XVII (1); see also discussion on NT below.

<sup>200</sup> Appellate Body Report on *European Communities –Measures Affecting the Prohibition of Asbestos and Asbestos Products*, WT/DS/135, adopted on April 2001.

<sup>201</sup> *ibid* para 99.

<sup>202</sup> Mathur (n79) 14.

<sup>203</sup> The General Agreement on Trade in Services Art V; see discussion in subsection (e) below.

<sup>204</sup> *ibid* Art VII.

are no surprises in trade thereby making MFN a powerful tool of liberalisation and increasing the level of trade in services.

Nevertheless, MFN encourages ‘free rider countries’<sup>205</sup> which may portend favourable and unfavourable situations to developing depending on whether they are granting the market access or not. It is favourable if they benefit from concessions they are not party to but not the other way round. Nigeria’s 1998 schedule affirmed the country’s commitment to MFN treatment to all countries but noted that negotiations were in progress in ECOWAS where she is a member.

Transparency is the second general commitment in the GATS containing extra provisions which has the same significance with most WTO agreements<sup>206</sup>. It mandates that members should publish promptly (except in case of emergency) all relevant laws, regulations and measures affecting trade in services at the time of entering into force<sup>207</sup>. It also requires members to annually update the Council for Trade in Services about new laws, regulations, or guidelines that may significantly affect scheduled services<sup>208</sup>. This serves the purpose of informing and giving the Council opportunity to review and assess<sup>209</sup> its compatibility with the member’s schedule *viz-a-viz* their GATS obligations.

The GATS further requires members to establish ‘enquiry points’ within two years of the agreement from where other members can obtain regulatory information.

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<sup>205</sup> Landau (n106) 10; countries benefit automatically from concessions they are not a party to.

<sup>206</sup> See discussion of transparency in WTO in s3.1.2 (d).

<sup>207</sup> The General Agreement on Trade in Services Art III (1).

<sup>208</sup> *ibid* Art III (3).

<sup>209</sup> Thomas Cottier and Krista N Schefer, ‘The Relationship Between World Trade Organization Law, National Law and Regional Law’ (1998) 1 JIEL 83, 87.

They are also obliged to respond promptly to requests though this does not include the obligation to disclose confidential information that may be detrimental to public interest or the impede enforcement of law<sup>210</sup>.

There are three additional duties under the general obligations of members in Part II of GATS. First is the provision of access to domestic judicial, arbitral or administrative processes for affected service suppliers for review and remedy where there is decision affecting trade in services<sup>211</sup>. Secondly, the Agreement mandates consultations on issues relating to restrictive business practices on request with full and sympathetic consideration<sup>212</sup>. Finally, there should be mandatory and sympathetic consideration of subsidies adversely affecting other members<sup>213</sup>.

The GATS provisions in this regard require notification, allowance for comments, due process and publication of laws which reinforces domestic regulatory transparency<sup>214</sup>. The absence of ‘regulatory transparency’ had often been a factor inhibiting the entry of foreign investment into insurance markets of developing countries<sup>215</sup>. Unlike most developed trade partners, developing countries are just

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<sup>210</sup> The General Agreement on Trade in Services Art III *bis* .

<sup>211</sup> *ibid* Art VI (2); see s3.2.2 (d) for detailed discussions on domestic regulations.

<sup>212</sup> *ibid* Art IX.

<sup>213</sup> *ibid* Art X (2).

<sup>214</sup> *ibid* 51 .

<sup>215</sup> Skipper (n80)18; UNCTAD, Report of Ad Hoc Expert Meeting on Insurance Services, (2006) UNCTAD/DITC/TNCD/2006/1 para 15 <[http://www.unctad.org/en/docs/sddins12\\_en.pdf](http://www.unctad.org/en/docs/sddins12_en.pdf)> accessed on 22<sup>nd</sup> April 2011; UNCTAD, Trade and Development Aspects of Insurance Services and Regulatory Frameworks Note by the UNCTAD secretariat, (2005) para 22 UNCTAD/DITC/TNCD/2005/1715 <[http://www.unctad.org/en/docs/ditctncd200515\\_en.pdf](http://www.unctad.org/en/docs/ditctncd200515_en.pdf)> accessed 23<sup>rd</sup> April 2011.

being forced to adopt this principle owing to their trade obligations in international organisations.

Developing countries opening up their markets usually have to adapt their regulatory process and structure, trade rules and practises to meet the transparency requirement of the WTO<sup>216</sup>. The fear of having their usually protectionist domestic and trade policies criticised through reviews or opening their underdeveloped markets to world trade is often too much to comprehend by these countries. This coupled with the small nature of domestic markets of developing countries account for this reluctance.

Transparency is an important element of liberalisation and development under the WTO/GATS legal framework. It has the potential of opening up the legislative and regulatory processes of countries and therefore helps in accessing the governance systems in place<sup>217</sup>. Transparency is also ‘one of the most important principles of regulatory reforms fundamental for good governance’<sup>218</sup>. This principle would provide an ideal model of legal reforms in the NII, for the purpose of liberalisation. It offers both the supervisory and regulatory framework models leading to higher levels of credibility and legitimacy which ensure a positive development of the sector. It enables the gains of trade to accrue through the entrance of more investors both local and foreign with investment capital and skills because of the credibility which it affords.

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<sup>216</sup> E.g China.

<sup>217</sup> Julian Arkel, *Insurance Developing Countries: Some Issues for Consideration* in UNCTAD, *Trade and Development Aspects of Insurance Services and Regulatory Framework* (2007) UNCTAD/DITC/TNCD/2007/4, 316 <[http://www.unctad.org/en/docs/ditctnkd20074\\_en.pdf](http://www.unctad.org/en/docs/ditctnkd20074_en.pdf) > accessed 23<sup>rd</sup> April 2011.

<sup>218</sup> Delimatsis (n124) *ibid*; Kaufmann and Weber (130).

Transparency accentuates liberalisation efforts and it is a strong indicator of levels of liberalisation of financial markets especially in the aftermath of the recent global financial crisis which put it on the agenda of regulators all over the world<sup>219</sup>. As suggested by Kaufmann and Weber<sup>220</sup>, transparency requires a three-dimensional approach which are the institutional aspects i.e. procedures and decision making; the substantive aspects which is the anchor of financial regulation establishing trust by providing legal certainty; and the accountability of financial market actors<sup>221</sup> for rebuilding confidence in the financial system. It is pertinent to stress that accountability of both public and private actors is key in this regard and this can only be facilitated by independent institutions and expert networks<sup>222</sup>. This works well with the polycentric form of PBR discussed earlier which requires mutual trust for success<sup>223</sup>.

Transparency as a model regulatory principle for liberalisation of insurance facilitates ‘inter-jurisdictional trust<sup>224</sup>, amongst regulators from different jurisdictions and confidence is built on openness about each other’s rules and regulations. This fact is also relevant in the NII because sound disclosure is the foundation for confidence in insurance markets<sup>225</sup>. Therefore, in the current scheme of global regulatory integration, global trade and the entrenched reciprocity principle, developing countries may have to incorporate the three

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<sup>219</sup> Kaufmann and Weber (n130) 780

<sup>220</sup> *ibid* 780-7.

<sup>221</sup> These include state and financial institutions on one hand financial institutions, investors and customers on the other.

<sup>222</sup> The discussion on supervisory independence in chapter two is relevant in this context; Kaufmann and Weber (n130) *ibid*.

<sup>223</sup> See discussion on PBRs in s2.4

<sup>224</sup> Skipper (n80)52.

<sup>225</sup> Yoshi Kawai, ‘IAIS and Recent Developments in Insurance Regulation’ (2005) 30 GPRI 29, 31.

aspects of the transparency principle in their regulatory reforms and face the reality of market opening to facilitate an improved domestic economy. Though there are problems associated with liberalizing and opening up of domestic markets, the benefits are often high as long as this is preceded by adequate regulatory and supervisory infrastructure as stated earlier<sup>226</sup>.

### *Specific Commitments*

Part III of the GATS comprises specific commitments and provisions governing the scheduling of these commitments<sup>227</sup>. As earlier noted, members who take on specific liberalisation commitments under NT and Market Access have this listed in their schedule of commitments. It is a guarantee to suppliers in other countries that conditions of entry and operation in the market would not change to their disadvantage<sup>228</sup>. Members are not obliged to grant access to foreign suppliers or provide NT outside those inscribed in their national schedules<sup>229</sup> following the bottom-up approach. The implication is that members have accepted commitments to provide market access for trade in services only in specified sectors and sub-sectors<sup>230</sup>. Consequently, market access and NT stated in the schedules of members form the basis for evaluating adherence to commitments.

Market access provisions require that each Member:

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<sup>226</sup> See discussion in chapter one and two on gains of liberalisation.

<sup>227</sup> The General Agreement on Trade in Services Art XVI to XVIII (2).

<sup>228</sup> WTO 'Guide to Reading Schedules' (n189).

<sup>229</sup> Juan A. Marchetti and Petros C. Mavroidis, 'What are the Main Challenges for the GATS Framework? Don't Talk About Revolution' (2004) 5 EBOR 511, 515; see above s4.1.2.

<sup>230</sup> Chakravarthi Raghavan, 'Financial Services, the WTO and Initiatives for Global Financial Reform' < <http://www.g24.org/TGM/cr0909.pdf> > 23, accessed 17<sup>th</sup> July 2012.

*“shall accord services and service suppliers of any other Member treatment no less favourable than that provided for under the terms, limitations and conditions agreed and specified in its Schedule”*<sup>231</sup>

The above provision applies like in all WTO agreements<sup>232</sup> but with more flexibility in the GATS because members’ are allowed limitations provided they do not fall under prohibited limitations<sup>233</sup>. These are qualitative or quantitative restrictions such as on the number of suppliers, total value of service transactions, total number of service operations or total quantity of service, on number of natural persons employed, on requirement of specific type of legal entity and maximum participation of foreign capital.

Market access does not prevent members from implementing measures legitimately in pursuit of national policies provided it is stated in the country’s schedule of commitments as limitations. Though the GATS allows limitations, it expressly prohibits measures that hinder the ability of foreign service providers to determine the desired form of establishment either by requiring a new juridical person or even limiting the amount of capital to invest<sup>234</sup>. In some jurisdictions this may come through a registration requirement that includes setting up of offices and determining how the board or management is constituted. An example exists in the NII where only limited liability companies are licensed as insurance

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<sup>231</sup> The General Agreement on Trade in Services Art XI (1).

<sup>232</sup> See discussion on market access above in s3.1.2 (a).

<sup>233</sup> The General Agreement on Trade in Services Art XVI subsections (2) (a)-(f).

<sup>234</sup> *ibid* Art XVI (2).

service providers.

However, some protectionist policies go beyond regulations therefore as a regulatory model, market access requires elimination of both explicit and implicit restrictions and barriers from standards and domestic regulations<sup>235</sup>.

NT obligations in the GATS are provided as follows:

*“In the sectors inscribed in its Schedule, and subject to any conditions and qualifications set out therein, each Member shall accord to services and service suppliers of any other Member, in respect of all measures affecting the supply of services, treatment no less favourable than that it accords to its own like services and service suppliers.”*<sup>236</sup>

From the above, NT obligation is subject only to scheduled sectors<sup>237</sup> and conditions under the GATS. Therefore signatories may engage in discriminatory policies for sectors as long as it does not include those in its schedule of commitments. The irony is that NT which had been viewed as having a limiting effect on regulatory autonomy of countries since the inception of multilateral trading system in 1948<sup>238</sup> has been limited to scheduled commitments in services trade because of the need for greater regulations. This had therefore allayed the fears of developing countries that had kicked against the inclusion of services in the world trading system.

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<sup>235</sup> Mathur (n85) 25.

<sup>236</sup> The General Agreement on Trade in Services Art XVII (1).

<sup>237</sup> See discussion of sectors in s3.2.1(a) above.

<sup>238</sup> Debra P Steger, ‘The Culture of the WTO: Why it Needs to Change’ (2007) 10 JIEL 483, 488.

Additionally, the same definition of ‘service suppliers of any other member’ holds as the analysis in s3.2.1 above subject to the proviso of subsections (2) and (3) below. The scheduling guidelines<sup>239</sup> also states that NT obligations needn’t be taken outside the territory of the scheduling member. Therefore unlike under MFN, the definition of ‘service supplier of any other country’ in GATS is restrictive.

Article XVII Subsection (2) of GATS further provides that

*“A Member may meet the requirement of paragraph 1 by according to services and service suppliers of any other Member, either formally identical treatment or formally different treatment to that it accords to its own like services and service suppliers.”*

This allows members to use formally identical or formally different treatment on its own services in order to fulfil its NT obligations. This envisages that giving identical treatment to both domestic and foreign suppliers may result in unfavourable treatment to foreign suppliers. Therefore, different treatments may correct this imbalance and allow the member to fulfil its NT obligations.

Article XVII Subsection (3) further explains the test for less favourable treatment.

It states that

*“Formally identical or formally different treatment shall be considered to be less favourable if it modifies the conditions of competition in favour of*

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<sup>239</sup> WTO, ‘Guidelines for the Scheduling of Specific Commitments under The General Agreement on Trade in Services (GATS) (2001) Document S/L/92 of 28 March 2001 adopted by the Council for Trade in Services in 2001  
<[http://www.americanbar.org/content/dam/aba/migrated/cpr/gats/s\\_1\\_92.authcheckdam.pdf](http://www.americanbar.org/content/dam/aba/migrated/cpr/gats/s_1_92.authcheckdam.pdf)> accessed 23<sup>rd</sup> April 2011.

*services or service suppliers of the Member compared to like services or service suppliers of any other Member.”*

A treatment is less favourable if such modifies the conditions of competition to the detriment of like foreign services or suppliers. Therefore, any treatment not modifying competition would not qualify as less favourable. Nonetheless, members can use formally identical or formally different treatment measures provided this does not tilt competition in favour of like domestic suppliers or their services. From the above analysis, NT covers both de facto and de jure measures as explained under the MFN analysis above. What then are ‘like domestic suppliers or their services’?

The Panel in the *EC-Banana*<sup>240</sup> using the economic standard approach<sup>241</sup> had stated that the standards of likeness applicable in Article XVII of GATS derive from Article III of GATT which in *EC-Asbestos*<sup>242</sup> has been defined as ‘equality of competitive conditions for imported products in relation to domestic products’. Therefore, the important characteristic to determine likeness is the existence of ‘competitive relationship’ and ‘substitutability<sup>243</sup>’ between foreign and domestic supplier of services. There seem to be confusion as to the extent to which criteria used in GATT can be applicable in the GATS. The GATT uses four (4) main criteria which are; the use of physical properties; the international classification of

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<sup>240</sup> Panel Report on *European Communities - Regime for the Importation, Sale and Distribution of Bananas (EC – Bananas III)*, WT/DS27, para 7302.

<sup>241</sup> Diebold (n92); Diebold (n198) 5-8.

<sup>242</sup> Appellate Body Report on *European Communities – Measures Affecting the Prohibition of Asbestos and Asbestos Products*, WT/DS/135, adopted on April 2001, para 90.

<sup>243</sup> Aaditya Mattoo, ‘National Treatment in the GATS: A Cornerstone or Pandora’s Box’ (1997) WTO staff WP TISD-96-002, 24-5<  
<[http://www.wto.org/english/res\\_e/reser\\_e/tisd9602\\_e.htm](http://www.wto.org/english/res_e/reser_e/tisd9602_e.htm)> accessed on 23rd April 2011.

products; end-uses of product; consumer tastes and habits<sup>244</sup>. The first two criteria may be inappropriate for the determination of likeness in services because of the issue of intangibility<sup>245</sup>. However, end-uses of products and consumer tastes and habits have been said to be applicable criteria for likeness. End-uses seem to offer the most appropriate criteria because it allows for the test of competitiveness or substitutability<sup>246</sup> in the market through a calculation of the cross-elasticity of demand for the two products. The consumer tastes and habits also allows for comparison based on the ‘interpersonal relationship between service supplier and the consumer, which is inherent in the concept of services’<sup>247</sup>. Mattoo however posits that nothing in Article XVII suggest that modes of supply should be considered in determining likeness of services therefore if this is excluded, a ‘built in protection’ would be available to foreign service providers within the GATS agreement<sup>248</sup>. The GATS balance the opportunities for both the domestic market and the foreign service-providers by emphasising equal treatment for like goods irrespective of mode. It is of utmost importance therefore that domestic laws and measures emphasise NT requirements in liberalising economies.

In determining likeness of service suppliers, the *EC-Banana* panel interpreted Article XVII to include a consideration of potential service suppliers as service suppliers; a decision upheld by the Appellate Body<sup>249</sup>. This meaning is not consistent with the GATS definition of service suppliers which does not consider potential service suppliers. This contradiction would need clarification in future

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<sup>244</sup> Krajewski ‘National Regulation and Trade Liberalization’ (n4) *ibid*.

<sup>245</sup> *ibid* 99.

<sup>246</sup> Mattoo(n243) 25.

<sup>247</sup> *ibid* 15.

<sup>248</sup> *ibid*.

<sup>249</sup> *EC-Banana*, (n240) para 7.320 and (n242) paras 227-228.

cases before dispute panels. From the analysis above, the interpretation of ‘likeness’ and ‘treatment no less favourable’ follows the economic standard of interpretation used under MFN<sup>250</sup>.

Another pertinent issue is whether to apply ‘disjunctive tests’ or ‘cumulative tests’ of likeness. It is suggested by Krajewski that a disjunctive test which tests for likeness of services separately from that of likeness of service supplier would avoid the unfavourable results from a cumulative test<sup>251</sup>. However due to the inconsistent provisions of the GATS on the two non-discrimination elements, there is no agreement on whether in determining likeness the assessment required is that of the likeness of services or of service suppliers. This is yet to be effectively determined WTO jurisprudence<sup>252</sup> thereby making the indices for determining likeness inconclusive. Nonetheless, Diebold has submitted that the US competition law should be the basis of determining the competitive relationships in service trade in the GATS<sup>253</sup>.

However, a controversial aspect of NT is its application to subsidies as contained in the negotiating guidelines of 1993 and 2001 which stated that NT ‘applies to subsidies in the same way that it applies to all other measures’<sup>254</sup>. Consequently, members with discriminatory subsidies in place have two options provided by the

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<sup>250</sup> See discussion on general commitments above.

<sup>251</sup> Krajewski ‘National Regulation and Trade Liberalization’ (n4) 6.

<sup>252</sup> Diebold (n92) 188.

<sup>253</sup> *ibid.* chapter 14.

<sup>254</sup> WTO, ‘Guidelines for the Scheduling of Specific Commitments under The General Agreement on Trade in Services (GATS) (2001) Document S/L/92 of 28 March 2001 adopted by the Council for Trade in Services in 2001

<[http://www.americanbar.org/content/dam/aba/migrated/cpr/gats/s\\_1\\_92.authcheckdam.pdf](http://www.americanbar.org/content/dam/aba/migrated/cpr/gats/s_1_92.authcheckdam.pdf)> accessed 23<sup>rd</sup> April 2011.

negotiating guidelines which are either to schedule the subsidy as a limitation or bringing such subsidies in conformity with the provisions of Article XVII. A developing country like Nigeria however would be better off with scheduling subsidies as a limitation.

In summary, the GATS members are only obliged to apply the NT principle for those service sectors and the modes of trade it has committed. It is ‘understood as the avoidance of treating foreign suppliers differently than (like) domestic providers or services’<sup>255</sup> in sectors and modes where a member is already committed. Therefore, where a member commits both under the agreement on goods and on services, while it can just be automatically assured of NT for goods; it needs to negotiate NT for his commitments on services with its trading partners.

NT obligations apply for sectors inscribed on a country schedule to the extent of the conditions inscribed in it. The schedule of GATS subscribing member would list sectors which the country is committing in, and the modes indicating ‘unbound’ i.e. no obligations on market access or NT, ‘limitations’ i.e. has limitations inconsistent with market access and NT obligations or ‘none’ where the country has full market access and NT obligations without limitations. This means that limitations to the different modes of supply in committed services not stated on the schedule is illegal.

Generally, NT ensures that members do not use internal measures to offset their liberalisation commitments in the GATS. However, ‘identical or different

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<sup>255</sup> David Snyder, ‘Free Trade in Insurance and Domestic Insurance Regulation in Harmony or in Conflict?’ (2007) 26 JIR 115, 117.

treatment' is permitted so long as 'conditions of competition' do not favour domestic service or their providers<sup>256</sup>. This implies that as a liberalisation model, GATS emphasis effective competition with level playing ground and not competition favouring domestic providers.

Complementing the distinction of obligations under general and specific commitments above is the 'bottom-up' or 'positive list' approach, where 'countries undertake national treatment and market access commitments specifying the type of access or treatment offered to services or service suppliers in scheduled sectors'<sup>257</sup>. GATS members assume coverage of only those areas actually listed, while all others are considered excluded. This undertaking of sector-specific access obligations narrows the NT obligations of countries to sectors listed in their schedules. In essence no country is obliged to apply NT principles to sectors or modes it has not committed to. The way this operates is that a member signifies the sector(s) it is willing to commit and this is a sort of invitation to other members to make offers in that area through negotiations. This is a very tidy approach and no country is pressured into making commitments in sectors it is not ready. The opposite of this would be a top-down approach that assumes a country is willing to commit in all sectors except those listed in its schedule.

The GATS is a development friendly platform and model that allows flexibility which enable countries choose in which sector or mode of supply to negotiate NT

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<sup>256</sup> Skipper (n80) 31.

<sup>257</sup> Sherry M Stephenson and Fransisco Javier Prieto, 'Evaluating Approaches to the Liberalization of Trade in Services: Insights From Regional Experiences in the Americas' (2001) 2 <[http://www.oas.org/en/sedi/dedtt/trade/pubs/steph02\\_Evaluat.pdf](http://www.oas.org/en/sedi/dedtt/trade/pubs/steph02_Evaluat.pdf)> accessed 23<sup>rd</sup> April 2011.

obligations<sup>258</sup>. Members are able to control their level of liberalisation a fact that informed the use of the WTO/GATS framework as the proper framework for greater liberalisation of insurance in Nigeria for economic development.

The liberalisation of the NII does not imply a total elimination of all restrictions on market access and NT but a carefully sequenced process of progressive liberalisation preceded by regulatory and supervisory reforms which is modelled after the regulatory principles enshrined in the GATS.

Currently Nigeria's schedule of commitments does not reflect any progressive liberalisation since 1998 when insurance was included in its schedule. Despite increasing levels of autonomous liberalisation in the insurance sector no further commitment has been made in the GATS. Nigeria continues to be unbound in both consumption abroad and temporary entry modes of trade in most insurance subsectors except for services auxiliary to insurance.

The country has binding commitments in market access for life, accident and health insurance in commercial presence mode and remains unbound in other modes. Whereas for NT in these subsectors, the country is only bound in cross border and commercial presence mode with no limitations inscribed.

For reinsurance however, the approval of the minister of finance is required for market access but unbound for NT in the commercial presence while 20% compulsory cession is made to NigeriaRe on a first-refusal basis. Nonetheless, in

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<sup>258</sup> Hunter Nottage, 'Trade and Competition in the WTO: Pondering the Applicability of Special and Differential Treatment' (2003) 6 JIEL 23, 36.

market access for reinsurance and retrocession, no limitations exist on NT in cross border or consumption abroad mode. In reality however, there are measures in place restricting trade in this sector<sup>259</sup>.

In services auxiliary to insurance such as broking and adjusting, Nigeria has market access and NT commitments in all modes except for temporary entry of natural persons mode.

General restrictions in the schedule include mandatory insurance of all imports locally by Nigerian registered insurance companies, requirement for all brokers to get approval before signing contracts with foreign insurers and the insurance of all government assets by NICON.

Currently, the restrictions on insurance of all government assets by NICON and 20% compulsory cession to NigeriaRe have been abolished in practice but still reflect in Nigeria's schedule. Similarly restrictions are in place with regards to cross border trade in reinsurance and services auxiliary to insurance in market access obviously in violation of Nigeria's obligation. Nonetheless, the EU made requests for the elimination of needs test and compulsory cession for commercial presence mode. A consideration of the elimination of needs test may encourage foreign reinsurers into the country thereby reducing capital outflows in respect of reinsurance payments abroad.

Nigeria is relatively open but it would be beneficial for the country to make market access and NT commitments in sectors where unilateral liberalisation had been

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<sup>259</sup> See discussion in s5.3.

made in her future multilateral commitments because this would help ‘underpin essential macroeconomic and regulatory reforms which would provide a signal of stability to potential foreign investors and may also induce other countries to do same<sup>260</sup>.

Liberalisation of the temporary entry of natural persons mode would also be beneficial due to the dearth of skilled manpower in the NII because this may attract reciprocal commitments from trading partners in services which Nigeria has excess manpower such as educational services. The EU made requests in this regard on horizontal commitments for services auxiliary to insurance<sup>261</sup> and in financial services<sup>262</sup>. The Nigerian government needs to make offers in areas such as life business which continues to record poor performances and in special classes like aviation where the underwriting capacity is inadequate to cover the domestic risk situation. This move would allure foreign providers with capital; experience skills to NII who will help develop these lines of business.

## **b. Progressive Liberalisation**

This is a central and overriding objective and goal of GATS<sup>263</sup> forming an integral part of service negotiations<sup>264</sup>. It is one of the ‘fundamental principles upon which

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<sup>260</sup> Masamichi Kono et al, Opening Markets in Financial Services and the Role of GATS’ WTO Special Studies, 5 < [http://www.wto.org/english/res\\_e/booksp\\_e/special\\_study\\_1\\_e.pdf](http://www.wto.org/english/res_e/booksp_e/special_study_1_e.pdf) > accessed 23rd April 2011.

<sup>261</sup> GATS 2000 Request from the EC and its Member States to Nigeria: Horizontal Commitments, 3.

<sup>262</sup> *ibid* Financial Services, 1.

<sup>263</sup> Bernard Hoekman, ‘Tentative First Steps: An Assessment of the Uruguay Round Agreement on Services’ (1995) World Bank Policy Research WP 1455, 25 <<http://elibrary.worldbank.org/docserver/download/1455.pdf?expires=1303564279&id=id&accna me=guest&checksum=1FF1C20B2FB3EFAACA63BDBF2A9F6869> >; Aaditya Mattoo, and Pierre Sauve, ‘Domestic Regulation and Trade in Services, Key Issues in Aaditya Mattoo,

GATS resides<sup>265</sup> and also a philosophy that had been entrenched in multilateral trade negotiations since GATT<sup>266</sup> and followed through successive rounds eventually into WTO and GATS. Progressive or ‘step-by-step’<sup>267</sup> liberalisation is a means of achieving ‘progressive abolition of barriers to trade in services’<sup>268</sup> by progressively and individually lowering restrictions in consideration of socio-economic development<sup>269</sup> by members. The nature and extent of liberalisation of members under GATS is dependent on specific commitments under Market Access and NT and members are allowed ‘carefully determine the extent of liberalisation they wish to commit’<sup>270</sup>. This was the main attraction for developing countries at the onset of GATS.

The Agreement affirms the sensitivity and importance of services to global and domestic economies, but recognises that the pace of liberalisation may take longer in some economies and sectors than others because of variations in size and quality respectively. Hence, no country is expected to become liberalised in a hurry but it is the prerogative of each member to determine the speed of its liberalisation taking into consideration the various aspects of its economy. However, the GATS’ collective acceptance of a system of graduation in

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and Pierre Sauve (eds) *Domestic Regulation and Service Trade Liberalization*, (World Bank and OUP 2003) 1; Kelsey (n142) 28.

<sup>264</sup> Panagiotis Delimatsis, ‘Article XIX GATS: Progressive Liberalization’, in Rüdiger Wolfrum, Peter-Tobias Stoll and Clemens Feinäugle (eds) *Max Planck Commentaries on World Trade Law WTO-Trade in Services* (Vol 6 Martinus Nijhoff Publishers 2008) 1.

<[http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=1280263](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1280263)> accessed on 1<sup>st</sup> April 2011.

<sup>265</sup> Delimatsis ‘Due Process’ (n121) 17.

<sup>266</sup> Cottier (n103) 779.

<sup>267</sup> Arkell (n 210) 318.

<sup>268</sup> Panagiotis Delimatsis, ‘Determining the Necessity of Domestic Regulations in Services: The Best is Yet to Come’ (2008) 19 EJIL 365.

<sup>269</sup> *ibid.*

<sup>270</sup> Mina Mashayekhi, Elizabeth Tuerk and Deepali Fernandes, ‘Trade and Development Aspects of Insurance Services and Regulatory Frameworks’ in UNCTAD, *Trade and Development Aspects of Insurance Services and Regulatory Frameworks* (2007) UNCTAD/DITC/TNCD/2007/4, 26 <[http://www.unctad.org/en/docs/ditctnkd20074\\_en.pdf](http://www.unctad.org/en/docs/ditctnkd20074_en.pdf)> accessed 23<sup>rd</sup> April 2011.

liberalisation is articulated in Part IV of the Agreement in two ways<sup>271</sup> which are future negotiations, and regional and bilateral trade agreements<sup>272</sup>.

Liberalisation through negotiations aims at the gradual reduction of measures affecting trade in services on a ‘mutually advantageous basis’<sup>273</sup> with all parties benefitting. The guidelines and procedures for negotiations is drawn by the Council for Trade in Services after a general and sector specific assessment. Progressive liberalisation could also be through bilateral or regional agreement as noted above where countries could seek out other countries or group of countries with which they can have a mutually beneficial commitment thus giving negotiation methods an open definition.

Since there is no pressure or set time table for liberalisation under GATS<sup>274</sup>, each country determines when, how, what and with whom to commit. Hence, a member may choose to select sector and modes of supply, schedule market restrictions such as ‘limitation on insurance licenses’ or on foreign equity allowed, limit access to foreign insurers through national treatment limitations such as requiring residency for top managers or even schedule additional commitments<sup>275</sup>.

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<sup>271</sup> Kelsey (n142) 28.

<sup>272</sup> GATS Art V on economic integration require the deepening of existing levels of liberalisation through reduction and removal of discrimination among parties to the regional and bilateral agreements.

<sup>273</sup> The General Agreement on Trade in Services Art XIX.

<sup>274</sup> Compared to other alternatives, see discussion in introductory chapter above.

<sup>275</sup> UNCTAD, ‘Trade and Development Aspects of Insurance Services and Regulatory Frameworks: Note by the UNCTAD secretariat’ (2005) UNCTAD/DITC/TNCD/2005/17, 20 <[http://www.unctad.org/en/docs/ditctncd200515\\_en.pdf](http://www.unctad.org/en/docs/ditctncd200515_en.pdf)> Accessed 23<sup>rd</sup> April 2011.

The advantage that the GATS progressive liberalisation platform brings into liberalisation of services is the flexibility and regulatory freedom<sup>276</sup> it affords members. This flexibility could be horizontal<sup>277</sup>, vertical<sup>278</sup> or diagonal<sup>279</sup>. Most importantly, ‘there are virtually no obligations in the GATS that individual Members might find difficult to meet or, otherwise, elude under the relevant exemptions’<sup>280</sup>. The GATS respects the right of the members to regulate because both national policy objectives and level of development would be taken into consideration during negotiations. Though criticized by some scholars<sup>281</sup>, progressive liberalisation whether as a philosophy or principle dispelled the fears of imposition ‘of unacceptable level of foreign competition’<sup>282</sup>. It helps expand trade in services and promote economic growth and development of developing countries<sup>283</sup>.

The *US-Gambling* Panel decision acknowledges regulatory sovereignty of members as an essential pillar of progressive liberalisation though such sovereignty ends where the rights of other members are impaired<sup>284</sup>. Also in the *EC-Banana III* dispute, the WTO Appellate Body defined progressive

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<sup>276</sup> David Luff, ‘Regulation of Health Services and International Trade Law’ in Aaditya Mattoo And Pierre Sauve (eds) *Domestic Regulation and Service Trade Liberalization*, (World Bank and OUP 2003) 193.

<sup>277</sup> Rudolf Adlung, ‘Services negotiations in the Doha Round: lost in flexibility?’ (2006) 9 JIEL4 865, 867-8; this involves discrimination among WTO members through exemptions provided for MFN, recognition measures, economic integration and prudential measures under financial services.

<sup>278</sup> *ibid*, through variations in market access or national treatment across sectors or modes of supply by freely using any policy such as regulatory interventions

<sup>279</sup> *ibid*; this involves using member, sector or mode of supply divergences in trading conditions due to ‘non-harmonized regulatory approaches’.

<sup>280</sup> *ibid* 867.

<sup>281</sup> Gary Hufbauer and Sherry Stephenson, ‘Services Trade: Past Liberalisation and Future Challenges’ (2007) 10 JIEL 605, 611.

<sup>282</sup> WTO, ‘Services’ (undated) 30 <[http://www.wto.org/english/res\\_e/booksp\\_e/chap4\\_e.pdf](http://www.wto.org/english/res_e/booksp_e/chap4_e.pdf)> accessed 23<sup>rd</sup> April 2011.

<sup>283</sup> Delimatsis ‘Due Process’ (n121).

<sup>284</sup> Appellate Body Report on *U S - Gambling* (n 159) para 6.316.

liberalisation as involving ‘the removal of protectionist measures’, if even it is on a gradual basis<sup>285</sup>.

The GATS therefore offers a vehicle for progressive liberalisation on a non-discriminatory basis with the benefits of diversifying the financial sector in an efficient and stable manner<sup>286</sup>. As a liberalisation model for the NII, the government can gradually open the market in the most efficient and stable manner with well sequenced policies and reforms benchmarked against this framework without any pressure whatsoever.

### **c. Domestic Regulation Requirements**

Free trade rules in the post-world war era had been hinged on the understanding that trade liberalisation would not ‘infringe on upon domestic policy autonomy’ therefore the focus was border measures affecting trade liberalisation<sup>287</sup>. The Uruguay round of negotiations marked a shift in focus to ‘domestic regulatory and legal systems imbedded in the institutional infrastructure of an economy’<sup>288</sup>. However, GATS like some other agreements under the WTO shifted from negative integration in the GATT era to a positive integration. Thus, rather than stating what governments must not do, the emphases was on what government must do<sup>289</sup>.

The preamble to GATS recognizes members right to ‘regulate and introduce new

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<sup>285</sup> *EC—Bananas III* (n172) para 220.

<sup>286</sup> Kono et al (n260) *ibid*.

<sup>287</sup> Delimatsis ‘International Trade in Services’ (n124) 84.

<sup>288</sup> *ibid*.

<sup>289</sup> *ibid*, 85.

regulations' however, Article VI of the agreement encapsulates the domestic regulatory requirements of members. Though this article is titled 'Domestic Regulation' it contains measures as defined and discussed above<sup>290</sup> which are left to members to determine subject to certain principles of necessity<sup>291</sup>. This article relates to qualification requirements and procedures, licensing requirements and technical standards. Though Article VI recognizes that services require heavier regulation than any other product because of its inherent nature, members are required to make certain that they do not 'constitute unnecessary barriers to trade in services'<sup>292</sup>. Consequently, this article represents constraints on 'domestic regulatory prerogatives'<sup>293</sup> of the GATS members and safeguards against excessive regulations<sup>294</sup>. It does not constrain members' right to pursue appropriate and legitimate regulatory objectives because these are not the main focus of GATS but the measures by which these objectives are met is of interest<sup>295</sup>. The GATS affirms the principle of state sovereignty in conducting affairs in its territory in international law<sup>296</sup>.

The regulatory principles contained in the domestic regulatory requirements of members which form part of the regulatory standards and model being proposed by this thesis for the liberalisation of the NII are:

*i. Reasonableness<sup>297</sup>, Objectivity<sup>298</sup> and Impartiality<sup>299</sup>*

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<sup>290</sup> *ibid* 95; see also discussion in 3.2.1 (d) above.

<sup>291</sup> Cottier and Krajewski (n58) 826.

<sup>292</sup> Mashayekhi, Tuerk, and Fernandes (n270) 24.

<sup>293</sup> *ibid* 25.

<sup>294</sup> Cottier and Krajewski (n58) 827.

<sup>295</sup> GATS Preamble fourth paragraph; Adlung and Mattoo (n191) 66.

<sup>296</sup> Wouters and Coppens (n3) 208.

<sup>297</sup> GATS Art VI (1).

<sup>298</sup> *ibid* (2).

<sup>299</sup> *ibid* (1).

The GATS mandates that measures relating to the licensing, standards and qualification should not be trade restrictive but must be reasonable, objective and impartial. The analysis of these principles would highlight the scope and content of these provisions in sequence.

With regards the scope, these are procedural requirements for measures affecting trade in services with measures applying in the similar manner as analysed above. It refers to all actions whether legal or administrative affecting the purchase, use, payment, access or connection to a service. There are however two limitations to the application of these principles. First, they apply to sectors which members have taken ‘specific commitment’ and secondly, they are measures of ‘general application’. This indicates that it relates to measures applying to ‘unidentified number of cases’<sup>300</sup> and not specific situations<sup>301</sup>. However a measure applied in a specific situation that becomes a principle of general application falls under the ambit of this provision. Nonetheless, it is clear that only measures in committed sectors are expected to be administered in a reasonable, objective and impartial manner<sup>302</sup>.

However, a content analysis of these provisions requires a definition of these principles. Reasonableness is a basic requirement which connotes being within the standards of ‘rationality and sound judgment’<sup>303</sup>. Three tests commonly employed to test reasonableness are the ends/means, cost effectiveness and proportionality test<sup>304</sup>. In essence, the end of a regulation should be justified by the means

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<sup>300</sup> Delimatsis ‘Due Process’ (n121) 20

<sup>301</sup> Markus Krajewski, ‘Article VI GATS Domestic Regulation’ in Rüdiger Wolfrum, Peter-Tobias Stoll and Clemens Feinäugle (eds) *Max Planck Commentaries on World Trade Law WTO-Trade in Services* (Vol 6 Martinus Nijhoff Publishers 2008) 170.

<sup>302</sup> This is akin to the regulatory adequacy discussed in chapter two under regulatory challenges

<sup>303</sup> Krajewski ‘Article VI GATS’ (n301) 171.

<sup>304</sup> *ibid* 34, this is significant to our discussion of regulations for effective insurance liberalisation in

employed, it must be cost effective and necessary and finally it must not be disproportionate to the interest of the foreign supplier<sup>305</sup>. The forms of reasonableness usually expected of a liberalised economy are both substantive and procedural reasonableness guaranteeing reasonableness in both substance and process of government measures<sup>306</sup>. Reasonableness therefore ensures that the administration of domestic regulations is not unfavourable to international trade in services.

Objectivity ordinarily involves a process devoid of irrational, emotional or personal intentions<sup>307</sup> and it has to do with the regulatory objectives of individual members in their jurisdictions. Therefore, measures in the administration of domestic law are assessed in relation to the objective for which the law was made but not the substantive aspects in committed sectors. Impartiality however connotes not giving consideration or privileges to other parties or interests<sup>308</sup>.

These three requirements though closely linked are separate obligations which members must fulfil to avoid a violation of Art VI (1). They are absolute standards of treatment which unlike NT are not dependent on the treatment afforded domestic producers and do not require comparison with treatment to domestic supplier or investors. They however require the concept of rationality, proportionality, transparency, necessity and participation<sup>309</sup>. What this means in effect is that a measure or rule must take into consideration the effect on foreign suppliers' participation. A rule applying generally to both suppliers may not be

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s2.4.

<sup>305</sup> *ibid* 34-5.

<sup>306</sup> *ibid* 33.

<sup>307</sup> Krajewski 'Article VI GATS' (n301) 171.

<sup>308</sup> *ibid*; Delimatsis 'Due Process' (n121) 26.

<sup>309</sup> Ortino F, 'From 'Non-Discrimination' to 'Reasonableness': A Paradigm Shift in International Economic Law?' (2005), The European Union Jean Monnet Programme, WP 01/05, 33 <[http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=922524](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=922524)> accessed on 18<sup>th</sup> April 2011.

burdensome to domestic suppliers but may be very burdensome to foreign suppliers. Therefore, the reasonableness and objectivity requirements on domestic regulation have a higher burden than that of NT.

Consequently, as model for liberalisation of the NII the legal framework of the industry should reflect these conditions in committed sectors. It is important to stress that measures which adversely affect the foreign service-provider may be construed as unreasonable, non-objective or partial even though they apply equally to all suppliers.

#### *ii. Remedial Processes*

Members should have in place judicial, arbitral or administrative processes to provide remedies for administrative decisions affecting service providers to the extent of its consistency with the constitution and legal system. This provides for recourse to an objective and independent process for the prompt review or provision of remedies for unfavourable administrative decisions. There are no provisions for the institutional structure of the body thus leaving the structure to each member to determine.

There are also carve-outs in subsection 'b' of this provision which exempts countries with constitutions or legal framework that do not allow such bodies from these obligations. This carve out whittles down the potency of this provision because the provision of a review process may become optional. However, the need for an independent review mechanism is very important for international trade and corroborates the transparency and predictability required of a regulatory system. The use of administrative powers is often discretionary and an ability to

challenge such actions will further provide a certain amount of confidence and predictability about such systems.

The significance of having effective remedial procedures in the legal and institutional framework of the NII is that enhances the credibility of the system while ensuring that the gains of liberalisation through greater investor confidence in the industry. This obligation is however binding on all members of GATS with or without scheduled commitments.

### *iii. Prompt Authorization*

In committed sectors where authorization is mandatory for foreign suppliers, members are obliged to do so within a reasonable time. While no definition of reasonable time is given it is noted that obligations of this nature have attached some flexibility especially as it relates to developing countries<sup>310</sup>. This is considering the relative limited capacities inherent in the system. Authorization should be issued upon completion of application while information on the status of application should be provided without delay upon demand. This provision is of great importance bearing in mind that authorization is one of the means by which regulators or governments limit access into their markets from foreign suppliers. However because trade in services is a highly regulated sector, it is important that prompt authorization is made an obligation to ensure free trade since it is by the fact that binds members only in committed sectors.

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<sup>310</sup> Keiya Iida and Julia Nielson, 'Transparency in Domestic Regulations: Practices and Possibilities' in Aaditya Mattoo and Pierre Sauve (eds) *Domestic Regulation and Service Trade Liberalization*, (World Bank and OUP 2003) 17.

For effective liberalisation of the NII, the supervisory agency would be required to put in place a fast process of authorization and licensing so that foreign suppliers are not deterred with unnecessary bureaucratic bottlenecks.

*iv. Transparency and Objectivity of Licensing Requirements in Disciplines*

The main transparency provision of the GATS is contained in Article II however, Members are encouraged to develop disciplines which contain measure on procedures, qualifications and technical standards for licensing which are transparent, objective and not burdensome or become unnecessary barriers to trade in services<sup>311</sup>. These conditions are to be based on competence and ability to supply service<sup>312</sup>. Unlike the earlier three sections of this article, this provision relates to the substantive laws and regulations on licensing procedures. It portrays the expected character of regulations in member countries which are transparency, objectivity and ‘unburdensomeness’<sup>313</sup>. It also provides for an integration in laws by the Council for Trade in Services through appropriate bodies. This envisages a sort of program leading to the adoption of minimum measures for licensing and technical standards<sup>314</sup> through disciplines. This provision reinforces the desire for uniform licensing and qualification regulations globally which reflect transparency and objectivity in order to prevent unnecessary trade barriers and facilitate easy licensing of foreign firms.

These provisions are also indicative of the purposes of the disciplines to be developed in different service sectors. The GATS goal of transforming the

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<sup>311</sup> The General Agreement on Trade in Services Art VI (4).

<sup>312</sup> *ibid* (4)(a)

<sup>313</sup> *ibid*.

<sup>314</sup> *ibid*

principles of transparency, objectivity into disciplines ‘is to make these principles sufficiently specific so that they are effective, enforceable and operationally useful<sup>315</sup>. Unfortunately, efforts at developing measures in the current Doha rounds have not successful and this has led to the pessimism about the ability of translating regulatory principles into disciplines in all service sectors. Nonetheless as a model of reforms, transparency of licensing process together with objectivity, competency and ability to supply service are good principles which will improve the quality of regulations and efficiency of the insurance market. This is important because only efficient markets can compete in the global insurance trade.

*v. International Standards*

Members are not to use licensing, qualification and technical standards requirements to impair or nullify their commitments in sectors which they have already committed in a way which ‘could not have been reasonably be expected of the member ‘at the time commitments were made. In determining this, standards of relevant international organisations would be used as a basis.

The important elements of this provision are that nullification and impairment that couldn’t have been expected of the member is prohibited. This implies that employing regulatory measures to deprive trading partners the benefits of market access or NT that would have been derived from members’ specific commitments is unacceptable. Secondly, standards of relevant international organisations are to

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<sup>315</sup> WTO, ‘Background Information on the Agreement on Technical Barriers to Trade and the Agreement on Import Licensing Procedures’ S/WPPS/W/6, 29 February 1996, para 2; Delimatsis ‘International Trade in Services’ (n124) 114.

be used in assessing nullification or impairment in the absence of disciplines. Relevant international organisation means international bodies where membership is open to the relevant bodies of members<sup>316</sup>. For insurance services, relevant international organisations include for example, the IAIS, International Insurance Society (IIS), International Insurance Foundation (IIF), International Actuarial Association (IAA) or International Organization of Pension Supervisor (IOPS) to mention a few. However, the IAIS is more representative of insurance regulators globally therefore, the most acceptable and prominent of all the insurance international organisations.

The implication of this passage is that the GATS has no prescribed standards of its own but benchmarks against acceptable standards. Secondly, liberalisation under GATS is not based on GATS specific provisions but other standards of relevant international organizations as enumerated by the GATS itself. The effect of this is that international standard setting organizations are given recognition and members not part of such bodies get to be assessed by them. It is regrettable that most of those organizations are dominated by professionals from developed countries thus making developing countries disadvantage not being represented there. Consequently, the peculiar economic situations warranting some peculiar measures in developing countries may not have been considered while setting the so called international standards. It would have been an added benefit if the provisions in Article VI of GATS has a clause ensuring that only organizations where due representation of most members of GATS is assured would be considered for standard setting. Nonetheless, this provides the push for developing

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<sup>316</sup> *ibid* 124.

countries to become members and participate actively in international standard setting bodies.

Equally significant is the fact that the GATS provides a 'safe harbour' for members whose licensing, technical standards and qualification requirements conform with those of relevant international organisations<sup>317</sup>. The implication for developing countries is that standards of these organisations have become a benchmark or model for domestic regulations. This significantly accounts for the use of the IAIS core principles as part of the parameters for the model of reforms being proposed in this thesis.

Nonetheless, the provision on international standards is temporal in nature since it is used 'pending the entry into force of disciplines developed in these sectors'. The development of disciplines in subsection (4) is therefore envisaged though only accountancy services discipline has been successfully adopted but none in insurance. Therefore, international standards of international organisations are still the benchmark for testing conformity to obligations and also determining nullification or impairment of obligations in the GATS.

Basically, provisions in Article VI show the fragile relation between domestic regulation and service trade liberalisation. The need to maintain regulatory autonomy of members (in setting qualification standards and licensing) is

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<sup>317</sup> *ibid.*

juxtaposed with the need to expand trade in services. It also can be viewed as an attempt to identify trade restrictive measures not essential to regulatory objectives. While regulatory autonomy is essential to enable government adapt their regulations to domestic conditions it is sometimes conceals protectionist intentions. However, Article VI is provisional in nature because it is not able to complete all aspects of service liberalisation such as the provisions in Article VI: 4 for the adoption of disciplines.

However, the concern about the GATS rules infringing on regulatory autonomy is an on-going discourse<sup>318</sup>. It is pertinent to note that the preamble to GATS does recognise the right of members to regulate and introduce new regulations on services supply. As noted above, regulation is very sensitive and important due to the nature of services. Therefore, this thesis argues that the autonomy to regulate still lies with governments of members. However, in committed sectors, members may be forced to adopt some standardized or harmonized regulations as part of their commitment. This definitely impinges on the regulatory autonomy of states though this thesis argues that giving up of part of a country's rights is imperative for the effectiveness of the WTO. As individuals give up some certain rights to belong to a certain social group so member countries may have their rights to determine their socio-economic policies constrained by rules and principles of the multilateral platform. Therefore, GATS like all trade agreements in services intrude in basically 'internal domestic policy' and consequently requires countries to make 'trade-offs involving flexibility, domestic sovereignty and international

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<sup>318</sup> Andrew Lang, 'The GATS and Regulatory Autonomy: A Case Study of Social Regulation of the Water Industry' (2004) 7 JIEL 4,801; Krajewski 'National Regulation and Trade Liberalization' (n4) 56; Krajewski 'Public Services' (n151) 9-10.

trade<sup>319</sup>. This study argues that a little compromise with domestic sovereignty that ensures greater income and welfare is more beneficial than an unrestrained domestic sovereignty that fails to provide the basic necessities or guarantee the necessary freedoms for decent living for its people.

Therefore, it is imperative that the government of Nigeria exercises caution in balancing these trade-offs while making offers in the sectors. It would be necessary to ensure that regulatory requirements international standards and disciplines are in line with the regulatory objectives of the country in relevant sectors. This would be necessary because withdrawal may take a long and painful process once a commitment is made as stated earlier<sup>320</sup>.

#### **d. Economic Integration**

The GATS recognises economic integration agreements (EIA) in services in its liberalisation framework<sup>321</sup> and this operates as an exemption from the MFN provisions<sup>322</sup> because it allows a subset of members to liberalize trade in services among themselves. The agreement does not ‘prevent any of its Members from being a party to or entering into an agreement liberalizing trade in services’<sup>323</sup> provided it has substantial sectoral coverage does not apply new discriminatory measures and it eliminates existing discrimination. Some flexibility is allowed if developing countries are parties to the agreement in terms of compliance with the

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<sup>319</sup> Copeland and Mattoo (n36) 127.

<sup>320</sup> See earlier discussion on predictability in s3.1.2(d).

<sup>321</sup> The General Agreement on Trade in Services, Art V.

<sup>322</sup> See discussion on general commitments above.

<sup>323</sup> The General Agreement on Trade in Services Art V.

provisions above<sup>324</sup>. This provision has a broad interpretation because it does not limit such integration to customs union or free trade areas therefore, any form of economic integration is allowed. However agreements not compliant with the conditions set up in Art V do not qualify for MFN exemptions and may be a ground for action from other members unless the preferential measures in the EIA is extended to other members. This is because the conditions are mandatory in nature<sup>325</sup>. Nevertheless, there is ambiguity in this provision because the definition of ‘substantial sectoral coverage’ is not provided making it difficult to determine which sectors would be exempted. Similarly, this provision is not mode specific because it does not state what mode of supply is exempted. Furthermore, the requirement of elimination of discrimination amongst its members would be difficult to measure since there is no standard against which such liberalisation could be measured.

The significance of this provision in relation to the objective of using the GATS model for the liberalisation of the NII is that Nigeria's membership of regional trade organizations would not be affected by multilateral trade commitments. The country could still discriminate in favour of other members of ECOWAS and AU and perform its obligations towards Africa Re and African Insurance Organizations. Besides, there has been reluctance on the part of GATS members generally to challenge EIAs<sup>326</sup>. Consequently, as this thesis proposes, Nigeria can juxtapose its regional obligations with its GATS obligation concomitantly.

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<sup>324</sup> *ibid* (1) (a),(b).

<sup>325</sup> Thomas Cottier and Martin Molinuevo, ‘Article V GATS: Economic Integration’ in Rüdiger Wolfrum, Peter-Tobias Stoll and Clemens Feinäugle (eds) *Max Planck Commentaries on World Trade Law WTO-Trade in Services* (Vol 6 Martinus Nijhoff Publishers 2008) 170.

<sup>326</sup> *ibid* 128.

#### **e. Monopolies, Exclusive Service Providers and Business Practices**

GATS approves of monopolies<sup>327</sup> though it does not permit the abuse of such dominant positions or its use to undermine specific commitments outside their exclusive rights<sup>328</sup>. It also recognizes that apart from monopolies and exclusive service providers there may be some business practices that restricts trade in services and thus implores members to enter into consultations to eliminate such<sup>329</sup>. This may be viewed as competition boosting law in GATS but contains no real obligations rather a persuasive provision requiring the member to enter into consultations. It is important to note that the GATS disallow the activities of monopolies and exclusive providers which affect MFN and NT obligations respectively<sup>330</sup>.

However, public monopolies had been a great barrier to trade before the WTO in developing countries where they had been used as a capacity development strategy in such sectors as insurance and telecommunication. For example in insurance, a lot of developing countries in the 1960's and 1970's set up public monopolies in form of national insurance companies following UNCTAD's recommendations in 1972 and 1973<sup>331</sup>. The fact is that monopolies do not enhance fair competition which is the reason why the provisions of this article are very inappropriate for developing countries' liberalisation and development. There cannot be liberalisation without fair competition and it is therefore not surprising that most

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<sup>327</sup> The General Agreement on Trade in Services Art VIII.

<sup>328</sup> *ibid.*

<sup>329</sup> *ibid* Art IX.

<sup>330</sup> *ibid* Art VIII (1) &(5).

<sup>331</sup> UNCTAD Resolution 42/III of 1972 and 7/VII of 1973 encouraging LDCs to adopt import substitution strategies.

countries have privatised their public monopolies including Nigeria<sup>332</sup>.

#### **f. Increasing Participation of Developing Countries**

Aside the developmental function in its preamble, GATS also made provisions for developing countries as part of its framework for liberalisation. This would be facilitated by negotiating commitments under Specific Commitments (Part III) and Progressive Liberalisation (Part IV) of GATS with the aim of:

- (a) The strengthening of their domestic services capacity through access to technology on a commercial basis;*
- (b) The improvement of their access to distribution channels and Information networks; and*
- (c) The liberalisation of market access in sectors and modes of supply of export interest to them*<sup>333</sup>

Developed member countries are, to ‘the extent possible’ establish ‘contact Points’ within two years to facilitate access to information by ‘developing country Members' service suppliers to information’, related to their respective markets, and

- (a) Commercial and technical aspects of the supply of services;
- (b) Registration, recognition and obtaining of professional qualifications; and
- (c) The availability of services technology<sup>334</sup>.

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<sup>332</sup> In Nigeria, National Insurance Corporation of Nigeria (NICON) set up during this period for that purpose has been privatised during the federal government privatisation programme.

<sup>333</sup> The General Agreement on Trade in Services Art IV (1).

The Agreement also states that priority must be given to Least Developed Country members who may find it difficult to accept specific commitments due to their economic situation and financial needs<sup>335</sup>.

Overall, these provisions attempt to strengthen developing countries' domestic services capacity, efficiency and competitiveness through access to technology on a commercial basis; the improvement of their access to distribution channels and information networks; and the liberalisation of market access in sectors and modes of supply of export interest to them'. Also where developing countries are members of an economic integration, they are exempt from meeting the requirements under the provisions of the GATS.

This provision lacks potency because there is no obligation on the part of the developed country to consider any of the above despite the fact that the WTO has development as its main objectives. It is rather disappointing therefore that the provisions that are meant to ensure effective participation of two thirds of WTO lacks the authority to do so. Developed countries are only 'to the extent possible' make available 'contact points' to provide information to developing countries for trade purposes. The tone of this provision is characteristic of the tone of most of the SDT provisions for developing countries. Whilst the provision shows that developing countries have special needs, it does not provide a serious solution for them. There is no certainty about the effectiveness of this provision consequently; it may not be wise to rely on such for developmental purposes. Rather, there is

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<sup>334</sup> *ibid* Art IV (2).

<sup>335</sup> *ibid* (Art iv(3)).

certainty in negotiations and entering into binding commitments, an option which has been very difficult for developing countries to consider. Relying on preferential treatment is not a sure framework for development within WTO rather liberalising and negotiating commitment is. Therefore, for the liberalisation of the NII, the only SDT provision to be considered is technical assistance which is discussed next because this would be of more benefit in assisting Nigeria identify its interest and initiating negotiations along that line.

#### **g. Technical Cooperation**

Article XXV confirms the need and right to technical cooperation for developing countries by WTO secretariat by providing that “*Technical assistance to developing countries shall be provided at the multilateral level by the Secretariat*”.

This is recognizing the fact that development for countries not yet developed may require the WTO itself rendering some assistance. Therefore, a novel provision was made specifically for this assistance thereby placing on the shoulders of WTO secretariat the job of assisting developing countries achieve development through technical cooperation and assistance. Technical assistance is one of the two SDT provisions that are certain for developing countries which aims at enabling these countries enter into binding commitments. In this light, WTO secretariat has had to cooperate with UNCTAD<sup>336</sup> because negotiations in the WTO/GATS are so refined giving little consideration to peculiar ‘needs of the developing countries’<sup>337</sup>. UNCTAD was created to help ‘maximise the trade, investment and development opportunities of developing countries and assist them in their efforts

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<sup>336</sup> UNCTAD was created by the UN to help integrate developing countries into the world trading system.

<sup>337</sup> *ibid.*

to integrate into world economy on equitable bases<sup>338</sup>. It was instrumental to the inclusion of GSPs and SDTs<sup>339</sup> ‘a generalized, non-reciprocal, non-discriminatory system of preferences in favour of the developing countries in GATT’<sup>340</sup>.

Unfortunately, developing countries’ use of SDTs and trade restrictive measures as tools of economic development is inconsistent with the main principles of the WTO/GATS that promote liberalisation of trade. All SDT provisions in the WTO<sup>341</sup> aimed at non-reciprocal market access are unenforceable, non-mandatory, unpredictable and ineffective as a tool for economic development. The inability of WTO members to balance the legal structure of WTO agreements based on reciprocity and binding obligations for all members with the provisions on ‘technical and financial assistance and longer transitional periods for developing countries’<sup>342</sup> has made progress almost impossible even under current Doha Round of negotiations.

The GATS commitment to progressive liberalisation seems to be the sure path for developing countries in order to guarantee benefits to the economy. This is because a change of members’ rights and obligations under WTO is highly unlikely as this obligations form the cornerstone of the WTO. In the same vein, it

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<sup>338</sup> UNCTAD, ‘About UNCTAD’  
<http://www.unctad.org/Templates/Page.asp?intItemID=1530&lang=1> accessed 13<sup>th</sup> October 2009.

<sup>339</sup> GSP means a The Generalized System of Preferences.

<sup>340</sup> Gene M Grossman and Alan O Sykes, ‘A Preference for Development: The Law and Economics of GSP’ (2005) 4 WTR 41, 42.

<sup>341</sup> Mitsuo Matsushita, Thomas J. Schoenbaum and Petros C. Mavroids, *The World Trade Organization: Law, Practice and Policy* (OUP, 2006) 177.

<sup>342</sup> Donatella Alessandrini, ‘Making WTO More Supportive of Development? The Doha Round and the Political Rationality of the WTO ‘s Development Mission’ (2009) 1 Law, Social Justice & Global Development Journal, 8  
<[http://www2.warwick.ac.uk/fac/soc/law/elj/ugd/2009\\_1/alessandrini](http://www2.warwick.ac.uk/fac/soc/law/elj/ugd/2009_1/alessandrini)> accessed 19<sup>th</sup> October 2009.

is very unlikely that SDTs or GSPs would be approved uniformly for all LDCs following the debate on graduation<sup>343</sup>. The current global financial crises make it even difficult to consider forcing WTO members to grant preferences.

The flexibility allowed in GATS was as a result of the financial crises in Asia and US in the 1990s therefore, progressive liberalisation is the confident way that developing countries can benefit from the WTO. Recent global financial crisis has further increased the disparity between developed and developing countries on GSPs. This leaves LDCs with no other viable option for effective global trade participation than through liberalisation and commitment under WTO/GATS like China, India and South Africa had done before emerging economies to be reckoned with.

Besides evidence from recent research suggest that ‘developing countries with more liberal trade policies achieve higher rates of growth and development than countries that are more protective’<sup>344</sup>.

In realisation of the failure of GSPs and SDTs, UNCTAD through its ‘positive agenda’ currently works in partnership with WTO secretariat to give technical assistance to developing countries towards liberalisation. Significantly, UNCTAD’s move is aimed at improving the LDCs negotiating capacity more so when it is becoming increasingly obvious that LDCs’ continued request for assistance rather than commercial agreements with developed countries has failed to yield any positive fruit.

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<sup>343</sup> See discussion on reciprocity in s3.1.2.

<sup>344</sup> Grossman and Sykes (n340) 62

This affirms the fact that GATS remains an effective framework for liberalisation. It is in this light that WTO and GATS is being proposed as a legal framework for the liberalisation of NII with potential for growth.

Technical cooperation is a very important provision for developing countries' liberalisation because it provides the requisite assistance to meet the inadequacies relating to effective negotiations. As a liberalising framework for the NII, Nigeria needs to take advantage of this form of assistance to ensure that the liberalisation of the sector is eventually locked into commitments which will foster increasing trade and development for the NII and the economy at large.

#### **h. General Exceptions**

Basically, exceptions are allowed under GATS<sup>345</sup> like in other international agreements for securing and maintaining law and order<sup>346</sup>, to protect lives whether, human, animal or plants<sup>347</sup> and to secure compliance with laws not consistent with the agreement like fraud, privacy and safety are allowed<sup>348</sup>. These restrictions are allowed on trade in services and associated payments provided they are not used as a means of discrimination or disguised restriction on trade in services.

In the *US Gambling* case<sup>349</sup>, both the panel and appellate body agreed that general

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<sup>345</sup> The General Agreement on Trade in Services Art XIV

<sup>346</sup> *ibid* subsection (a).

<sup>347</sup> *ibid* (b).

<sup>348</sup> *ibid* (c).

<sup>349</sup> Panel Report *US –Gambling* (n284) para 6.448; Krajewski 'Service Trade Liberalisation' (24)172-3 .

exceptions had a ‘two tiered approach’ that needs to be tested against the requirements in the sub-paragraphs such as maintaining law and order, protection of lives etc. and also the fulfilling conditions of its introductory clause i.e. not to be used as means of discrimination or trade restriction.

A member is allowed to derogate from its commitments whether specific or general in order to meet non- economic objectives like law and order to the extent as that they become instruments of discrimination. This significance of this provision is that the WTO recognises that some situations may warrant derogation from obligations. Unfortunately, this has been abused by countries that use it to perpetuate protectionist or discriminatory policies.

Nevertheless, the significance of this provision for countries using the GATS framework for liberalisation is that derogation from commitment is allowed where domestic circumstances require them. Therefore where the NII liberalisation brings about some unfavourable non-economic consequences, government is able to put in measures to abate them<sup>350</sup>.

From the analysis of above, five approaches to liberalisation are identified with the GATS model<sup>351</sup>. These include:

- a. Ban on quantitative restrictions- this is legitimate in the GATS for as long it is not used in committed sectors<sup>352</sup>.

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<sup>350</sup> This may involve a long process; see discussion on predictability in s3.1.2.

<sup>351</sup> Wouters and Coppens (n3) 209.

<sup>352</sup> The General Agreement on Trade in Services Art XVI (2); see also discussion on market access in s3.2.2(a).

- b. Non-Discrimination in form of MFN and NT<sup>353</sup>.
- c. Mutual Recognition Agreements – this is a common way of achieving mutual recognition of qualifications and standards. This is significant to services liberalisation and it forms part of domestic regulation provisions<sup>354</sup> especially the development of disciplines and future objectives of the GATS. Mutual recognition is a very effective means of ensuring liberal access but it requires some level of regulatory convergence which may be difficult to achieve<sup>355</sup>.
- d. Harmonisation of Standards- this involves the setting of standards which are expected to comply with and which also inevitably limits the regulatory autonomy of members<sup>356</sup>. The GATS provide that ‘international standards of relevant international organisations’ are to be used as a measure of compliance to obligations in sectors where disciplines are not yet in force. Therefore, standards are interim instruments pending when disciplines would come into force. The irony though is that these standard setting bodies are also being consulted in construction of disciplines so they are and would continue to be relevant in the GATS.
- e. Necessity Test – this approach is relevant to the GATS domestic regulation regime especially non-discrimination obligations where both *de facto* and *de jure* discrimination are prohibited. It is a

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<sup>353</sup> See also discussion in s3.2.2 (a) below.

<sup>354</sup> The General Agreement on Trade in Services Art VI(4); see also discussion on Domestic Regulations in s3.2.2 below.

<sup>355</sup> Sumantha Chaudhuri, Aaditya Mattoo and Richard Self, ‘Moving People to Deliver Services: How Can the WTO Help’ World Bank Policy Research WP3238 (March 2004) 17.

<sup>356</sup> Wouters and Coppens (n3) 209.

‘positive obligation’<sup>357</sup> that measures should not be more trade restrictive than necessary to achieve domestic regulatory objectives.

From the above analysis it is evident the GATS model presents a number of approaches to liberalisation and provides both the platform for gradual liberalisation and also regulatory principles upon which domestic regulatory reforms can be founded. It ‘does not call for harmonization of domestic regulations’ rather it ‘encourages sound regulatory institutions and practices domestically’<sup>358</sup>. However, because its developmental provisions for developing countries are grounded mainly on non- obligatory provisions, it is argued they are a non-reliable aspect of the framework. This thesis in alignment with Hudec<sup>359</sup> posits that binding commitment with technical assistance is a more reliable provision within this framework. This is the approach which is being proposed for the liberalisation of the NII.

### 3.3 CONCLUSION

The theoretical and the legal framework of the concept of liberalisation within the WTO/GATS have been laid in this chapter. This complements the conclusion in chapter two that a well regulated and supervised NII with competitive laws and well sequenced liberalisation would enhance the growth potential of the Nigerian economy. The chapter has also presented the GATS as a model framework for liberalisation with unique advantages over other frameworks for liberalisation of

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<sup>357</sup> *ibid* 210.

<sup>358</sup> Delimatsis ‘International Trade in Services’ (n124) 164-5.

<sup>359</sup> Hudec (n132)159-160

service.

However, this thesis will proceed with the analyses of other relevant standards of insurance regulations. The Annex on Financial Services (AFS) is the relevant agreement in the GATS that sets the standards and other specific conditions for liberalisation of insurance. There are also other widely accepted standard setting models of insurance regulation and liberalisation such as the Insurance Model Schedule which derives from GATS and the International Association of Insurance Supervisors (IAIS) Insurance Core Principles (ICPs) also a recognized standard of insurance supervision in GATS. These are examined in the next chapter to reveal their adequacy as a legal framework for liberalisation of insurance services in Nigeria.

## **CHAPTER FOUR**

### **GATS FRAMEWORK FOR INSURANCE LIBERALISATION**

#### **4. INTRODUCTION**

The last Chapter reviewed literature on the concept of liberalisation and its application within the context of the WTO/ GATS framework and concludes that this framework is an adequate Model to promote liberalisation of the NII for growth and development. This chapter examines specifically the GATS liberalising framework for insurance services. The aim is to enable the construction of parameters of effective legislative and supervisory infrastructures in liberalizing insurance for the purpose of economic development.

This analysis is in four sections starting with liberalisation framework for insurance services in the Annex on Financial Services (AFS) which is part of the legal framework of GATS. The second section considers other models deriving from GATS such as the Understanding on Commitments in Financial Services and the Insurance Model and Best Practices. The standard setting principles of the International Association of Insurance Supervisors (IAIS) is also analysed. The construction of parameters for insurance regulation and supervision is done in section three based on the analysis in this and the earlier two chapters. The final section concludes with the argument that liberalisation other than GSP provisions of WTO/GATS is an effective way to enhance domestic productivity, trade and growth in developing countries

## 4.1 FINANCIAL SERVICES IN THE GATS

The AFS represents agreements on financial services which is the largest of all service sectors. It contains five paragraphs out of which two are considered due to their relevance to the liberalisation framework of insurance within GATS. These are the definition of financial services and Prudential Carve-out (and its recognition).

### a. DEFINITIONS IN THE AFS

**Financial Services** - The AFS defines financial service as:

*“any service of a financial nature offered by a financial service supplier of a Member. Financial services include all insurance and insurance-related services, and all banking and other financial services (excluding insurance)”*  
(para 5(a))

From earlier definition of services<sup>1</sup>, financial services are services not supplied in exercise of government authority, for profit or in competition with other suppliers that has a financial nature. The AFS provides for situations where statutory duties of government (such as health and social security) or any other activities by a public entity using the guarantee or financial resources of government is conducted in competition with another public service or financial service supplier. These are deemed to be a service falling under the ambit of GATS. The AFS further clarified the fact that it is not the service being rendered or the nature of the provider that is important but whether there is competition or profitability implied there from.

However, financial services could be insurance or insurance-related services, banking or other financial services. The AFS further breaks financial services into sixteen but

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<sup>1</sup> See s3.2.1(a).

only four are insurance and insurance related and they are<sup>2</sup>:

(i) **Direct insurance (including co-insurance)**: This means insurance policies

written solely by an insurance provider or shared with other insurance providers.

(a) **life**- this means life assurance policies which provide benefit either for the one whose life is insured or his or her named beneficiaries whether the insured is alive or not including pensions.

(b) **Non-life** – these are sometimes called general insurances. They are a group of insurance policies that are not based on the life of an insured but used to provide indemnity in situations of loss or damage to the property of the insured. They include fire insurance, theft or burglary insurance, liability insurances, and accident insurances.

It is important to note that direct insurance providers are often either locally incorporated or registered having to meet the local requirements for setting up insurance business.

Trade in direct insurance is largely done on establishment mode of the GATS except for large specialist risks (like oil and gas insurance, aviation insurance, and marine hull insurance for large vessels) which may be insured internationally on cross-border basis. However, in economic union territories like EU, cross-border and consumption abroad is allowed in direct insurance trade.

(ii) **Reinsurance and retrocession**- these are second and third level insurance risk

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<sup>2</sup> Annex on Financial Services s5(a)(i-iv)

transfer. As stated in section 2.1 they are not involved in direct insurance but only insure policies already insured by direct insurance providers. In reinsurance and retrocession, the reinsurer does not have any legal liability towards the original insured but to the direct insurer. Trade in reinsurance and retrocession is usually either by local establishment or cross border. However, in a lot of developing countries, the bulk of reinsurance and retrocession is done on cross- border basis to ensure capacity building for domestic insurance markets because of their technical and capital inadequacies.

*(iii) Insurance intermediation, such as brokerage and agency* - these are the various intermediaries within the insurance market. They are either agents of the insured or the insurer depending on regulations and practice in various jurisdictions. These agents could be professional individuals or corporate bodies like brokers or others which are not necessarily insurance professionals. Sometimes non-professional insurance bodies could also act as agent such as when banks act as agent for insurance companies. Trade in insurance intermediation, is predominantly done on establishment, but trade on temporary movement of persons basis is often required for very large special risks especially while seeking the placement of such risks with foreign insurance or reinsurance service providers. In the NII, foreign insurance intermediaries are not permitted.

*(iv) Services auxiliary to insurance, such as consultancy, actuarial, risk assessment and claim settlement services* – these are services not particularly insurance in nature but are essential to insurance such as consultancy, claims assessment and management and actuarial services. Like insurance mediation, trade in services

auxiliary to insurance can be provided on establishment, cross-border or temporary movement of persons basis where the services of international loss adjusters are required for large claims.

The significance of this classification under the AFS is that it slightly modified the sectoral classification in the W/120 document<sup>3</sup> used generally in the GATS. The issues relating to insurance are:

- (a) accident and health insurance are included in "life" insurance in the W/120 document instead of "non-life" insurance as it is often done globally in insurance practice and the UN<sup>4</sup> and this is not clarified in the AFS;
- (b) pension fund management services are set apart from life insurance services and included in asset management services under "banking and other financial services" which again is not the practice in trade in insurance services similarly not distinguished under the AFS; and
- (c) Insurance Mediation which includes 'insurance broking and agency services' has been 'disaggregated'<sup>5</sup> from "services auxiliary to insurance under the AFS which clearly identifies some of those auxiliary services; namely consultancy, actuarial, risk assessment and claim settlement services.

The implications of this fact is that since GATS members are expected to schedule their commitments using the services sectoral classification, members scheduling

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<sup>3</sup> see discussion on the concept of services in s3.2.1(a).

<sup>4</sup> United Nations, CPC classification (Statistical Papers, Series M, No.77, 1991).

<sup>5</sup> WTO, 'Financial Services: Background Note by the Secretariat' S/C/W/72 (2 December 1998) para 10.

insurance commitments would need to state categorically that they are scheduling based on AFS classification. This is important for regulatory reforms in insurance because, the legal framework needs to reflect AFS classification which is more explicit and in line with global practices in insurance. Nigeria's commitment was scheduled using the sectorial classification therefore insurance broking is grouped under services auxiliary to insurance. This thesis suggests that the next scheduling of commitments by Nigeria ought to reflect the AFS classification which is more realistic.

**A financial service supplier** – this is defined as:

*“any natural or juridical person of a Member wishing to supply or supplying financial services but the term "financial service supplier" does not include a public entity”* (5(b) of the AFS)

Following the GATS agreement, a financial supplier could be human suppliers or corporate suppliers but excludes any public entity. Strangely a public entity could be a private entity carrying out the functions normally performed by public entities such as central bank or any monetary authority. Therefore, in countries where government supply financial services in competition with private or other public entities, such government services would be deemed a service and subject to the GATS and AFS rules. Government provision of mortgage services is an example of this which further widens the scope of GATS and AFS.

## **b. PRUDENTIAL CARVE OUT**

This is the most important article with regards to the liberalisation framework GATS and AFS. In recognition of the members' prudential and regulatory concerns and also

bearing in mind the financial crises of the 1980s and 1990s<sup>6</sup>, some provisions were put in AFS to modify the provisions of GATS agreement especially with regards to domestic regulations. It is referred to as the ‘Prudential Carve’ and it includes ‘measures to protect investors, depositors, policy-holders or others to whom a fiduciary duty is owed by a financial service supplier, or to ensure the integrity and stability of the financial system<sup>7</sup>. Therefore, in recognition of importance of the service sector and the need for regulation for the purpose of economic growth, financial stability and consumer protection, the annex excludes prudential domestic regulations from the lists of barriers. This ensures that governments regulations geared towards the above objective are not classified as trade barriers which GATS seeks to eliminate.

The broad wording and lack of a definition or an example, and the fact that it does not require the criteria of proportionality makes it a clear departure from the main GATS requirement for domestic regulations. It is pertinent to note that the main GATS provisions require that domestic regulation is ‘fair and objective’ with qualitative requirements. On the other hand, the AFS exempts financial services from those situations requiring prudential carve out and necessitates that regulations should only be for ‘prudential or investor protection purposes’. Members do not have to prove the necessity for a measure like under the main GATS agreement. The council for trade must however be notified in both situations.

This is significant for developing countries because it relieves them of the burden of

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<sup>6</sup> There were financial crises in a number of countries in Asia and the United States, Japan’s inflated stocks prices and real estate in the 1980s and US Savings and Loans Crisis that led to the collapse of the thrift industry all attributed to ineffective regulatory and supervisory regimes.

<sup>7</sup> GATS Annex on Financial Services para 2 (a); See also discussion in chapter two s2.4.

having to prove necessity for prudential measures and provides them the mandate to use measures which they deem necessary to protect their financial markets.

Finally, where this prudential carve out does not conform to the provisions of GATS, *‘they shall not be used as a means of avoiding the Member’s commitments or obligations under the Agreement’*<sup>8</sup>.

In reality, despite the above provision, prudential considerations make commitments negotiations difficult or deprive foreign firms the benefit of negotiated market access. However, AFS allows for both mutual and unilateral recognition of members’ prudential measures without recourse to other members. This re-emphasises the flexibility of the GATS framework in accommodating the use of prudential measures with a very simple process of at least a unilateral recognition. It strongly supports the argument that the GATS model of liberalisation is viable for the NII especially from the revelation in chapter two that prudential regulations is key to an efficient and effective insurance market.

However, the asymmetry in the negotiating objectives of developed countries and developing countries, negotiations on financial services took a long time to be concluded. Developed countries with their interests primarily as exporters of financial services aggressively pursued the objective of market opening while developing countries were ‘more defensive’ because only a few of them export financial services on a large scale. This delay led some developed countries to set out an ambitious basis for scheduling commitments as an appendage to the GATS referred to as the

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<sup>8</sup> *ibid* para 2(a).

Understanding on Commitments in Financial Services. This understanding is a recognised standard for insurance services liberalisation specifically addressing issues hindering trade in insurance services. Nigeria's commitments in insurance in the GATS are scheduled on this understanding. These and other standards are examined next.

## **4.2 OTHER STANDARDS OF INSURANCE REGULATION**

This section examines the standards deriving from the GATS model such as the understanding on financial services and the insurance model schedule and best practices. From earlier analysis of the GATS' domestic regulations<sup>9</sup>, it was revealed that standards of international standard setting organizations would be used as a basis of assessing the compliance of members' domestic regulations to GATS commitment. The IAIS is one of the globally accepted standard setting organisations in insurance therefore, its principles would also be examine.

### **4.2.1 UNDERSTANDING ON COMMITMENTS IN FINANCIAL SERVICES**

This was an initiative to ensure a greater level of liberalisation than what obtains under the AFS. It provides a standard list of liberalisation commitments which adopting members would include in their schedule as an alternative approach to specific commitments provisions of the GATS. The highlights of this understanding include a standstill commitment that no new restrictive measure would be brought, foreign suppliers' right to establish commercial presence and obligation not to discriminate in government procurement of financial services. Furthermore, adopting members are obliged to ensure adequate transfer of information in a way that foreign suppliers are not adversely affected. More importantly they shall permit non-resident

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<sup>9</sup> See discussion in s3.2.2 (c)

suppliers of financial services either directly or through agents under NT to supply insurance services for maritime shipping, commercial aviation or space launch, for goods in international transit, reinsurance and retrocession. Similarly, members are obliged to allow its citizens to purchase financial services from the territories of other members.

Quite a number of countries including Nigeria have undertaken commitments in financial services using the Understanding though they are not obliged to accept its entire elements. The Understanding is not in conflict with the main provisions of GATS and it applies on Non-discrimination basis.

However, because the Understanding was drawn mainly by and for developed countries the interests of less developed members of WTO were not considered. It reflects the dichotomy between the developed and developing countries with the former clamouring for more openness and greater liberalisation and the latter resisting this idea for various reasons based mainly on the infant industry argument<sup>10</sup>. It is therefore not surprising that Nigeria's 1998 commitments under the Understanding fell short of the minimum amount of openness. The monopoly of insuring all government properties were given to the government's company NICON. The country continues to increase restrictions under its Local Content Policy without consideration for the stand still commitment.

This thesis argues that developing countries are incapable of abiding with the Understanding's provisions for greater liberalisation due to structural problems

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<sup>10</sup> See discussion on challenges of liberalisation in s2.5.

associated with their poor development. This does not imply that the Understanding is inherently bad but that developing countries' legal and institutional framework cannot ensure positive gains from scheduling commitments under it.

#### 4.2.2 INSURANCE MODEL SCHEDULE AND BEST PRACTICES

##### Origin and Function

The insurance industry took part in the negotiations of the WTO Financial Services Agreement of 1997 often referred to as the 'Fifth Protocol of GATS'. They were represented by the Financial Leaders Working Group (FWLG) consisting of insurance associations and some other individual companies from developed countries<sup>11</sup>. Yet, when the GATS was concluded, the FWLG realised that the agreement could result in vague and contradictory commitments because there was no regulatory best practice<sup>12</sup>. Consequently, initial commitments were imprecise as envisaged<sup>13</sup>. This prompted the FWLG to develop 'Pro-Competitive Regulatory Principles for Insurance'. It represented principles of market access, NT and regulatory best practice which were considered significant for liberalised insurance markets wishing to combine prudential regulations with competition and so on<sup>14</sup>. Another reason for these principles was a realisation by foreign insurers that market access achieved at the negotiations was often lost to regulators<sup>15</sup> who use non pro-competitive prudential

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<sup>11</sup> They were from the Quad countries; Canada, the European Union, Japan and the United States.

<sup>12</sup> John Cooke, 'Approaches to GATS Liberalisation and the Challenges to Emerging Market' UNCTAD, *Trade and Development Aspects of Insurance Services and Regulatory Framework* (2007) UNCTAD/DITC/TNCD/2007/4, 372-3  
<[http://www.unctad.org/en/docs/ditctncd20074\\_en.pdf](http://www.unctad.org/en/docs/ditctncd20074_en.pdf)> accessed 23<sup>rd</sup> April 2011.

<sup>13</sup> Alastair Evans, 'International Trade in Financial Services and the GATS' in Kern Alexander and Mads Andenas (eds) *The World Trade Organisation and Trade in Services* (Martinus Nijhoff, 2008) 745, 748.

<sup>14</sup> Cooke (n12) 373.

<sup>15</sup> David Snyder, 'Insurance Service and Recent Trade Negotiations' in Kern Alexander and Mads Andenas (eds) *The World Trade Organisation and Trade in Services* (Martinus Nijhoff, 2008) 755, 760.

measures<sup>16</sup>. Unfortunately, the principles did not ensure the clarity needed for ‘framing more standardized schedules of commitments’ hence the decision to translate them into the ‘actual language of commitments on insurance under the GATS’ which resulted in the Insurance Model Schedule and Best practices<sup>17</sup>.

This model was intended to provide legal clarity for the forms of commitments that countries could take and also represent a structured way by which progress could be made in insurance services liberalisation<sup>18</sup>. It also translates the GATS insurance commitments into practical terms. The Best Practice proposed a set of model regulatory obligations which countries may adopt under additional commitments of GATS<sup>19</sup>. It was ambitiously thought of as an insurance service reference paper on the bases of which commitments in insurance services would be scheduled. It however failed to achieve that goal because it was not universally accepted like the Telecommunications Reference Paper.

Nonetheless, it still represents a regulatory model which guides the negotiating process in insurance services. The best practice is also a good regulatory model for reforms in domestic legislations. The two represent internationally recognised standards of insurance liberalisation deriving from the GATS framework further proving the viability of the framework for insurance services liberalisation. It presents an ideal model for liberalisation and best practices towards ensuring a viable insurance industry.

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<sup>16</sup> *ibid.*

<sup>17</sup> Cooke (n12) 373.

<sup>18</sup> Evans (n13) *ibid.*

<sup>19</sup> *ibid.*

## Insurance Model Schedule

The model makes provisions under the market access and national treatment as a reference point for countries wishing to liberalise their insurance sectors. It proposes that the text of the model is reflected in the schedules of members along with the obligations assumed under market access and national treatment and contains five parts discussed below.

The first part contains standstill measures like the Understanding on Financial Services while the second relates to cross border market access. This ensures market access without any form of restrictions to domestic or foreign insurance companies. Also, mandatory cessions which require direct insurance companies to cede a portion of their risk to specified insurance or reinsurance suppliers were eliminated. Other measures for eliminations are restrictions on cessions to foreign reinsurers or right of first refusal for domestic reinsurance suppliers. Discriminatory requirements like localisation of assets and collateralisation for foreign reinsurance suppliers were also to be eliminated. The essence of these provisions is for freer flow of trade and greater liberalisation. Reinsurance promotes geographical spread of risk and tying reinsurance funds to a particular location may affect the flow of such services bearing in mind retrocession<sup>20</sup> among reinsurers themselves.

The third part of the model relates to commercial presence mode of access dealing with issues of establishment, equity shareholding compulsory insurances, monopolies and pensions management. Provisions include foreign suppliers' ability to set up

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<sup>20</sup> See discussion in s2.1.

subsidiary with 100% equity, register a new company or acquire an existing company as a branch in the host country. Domestic regulations should recognise the relationship between the parent company and new company and foreign supplier can use its home company in the provision of services when not infringing on existing trademark. Similarly, it should not be denied access because of its legal nature at home.

Furthermore, in joint ventures, the percentage of equity shareholding of the foreign supplier should be determined solely by the parties themselves. Foreign equity share restrictions should be eliminated and the foreign partner should be allowed at least 51% of the company. Also proposed is the removal of restrictions preventing foreign suppliers' competing for compulsory insurance products. Measures encouraging monopolies or exclusive suppliers of insurance services should be eliminated. Similarly, foreign suppliers maintaining commercial presence should be allowed to participate in pension systems on non-discriminatory basis in jurisdictions permitting private participation. Therefore, the Insurance model supports the principles in the liberalisation model of the WTO/GATS.

The fourth part of the model relates to temporary entry mode of access where it proposes that requirements on nationality should be avoided. Furthermore, foreign suppliers in commercial presence should be at liberty to choose resident representatives irrespective of nationality once regulatory competency requirements are met. Also, temporary visa should be timely in this regard.

The final section on NT proposes that foreign suppliers are allowed to compete for insurances of state owned enterprises or enterprises where the state holds equity share like indigenous insurance suppliers. They should also not be treated ‘less favourably than domestic suppliers with respect to capital, solvency, reserve, tax and other financial requirements’. If prudential regulations are to be used as allowed under AFS, members would explain the basis for such and particularly why it is necessary for the protection of policyholders. Finally, in case of insurance intermediation, restrictions on transfer should only be limited to measures necessary for legal responsibilities in the country where they are delivering the service.

Most of the provisions of the model are in agreement with the main GATS framework but it is pertinent to note that requirement of explanation of prudential regulations is in excess of the AFS provisions on prudential carve out where unilateral or mutual recognition is required. No country should have to explain its use of prudential measures. The right to regulate is very much preserved under the GATS framework if it meets the domestic requirements in Art VI.

### **Best Practices**

This is to be assumed under Additional Commitments and it proposes additional commitments on transparency, solvency and prudential regulations, insurance monopolies and independent regulatory authority respectively.

New and existing regulation including revisions to existing law should be made publicly available in a public journal or register to all interested parties. Also, new or

revised laws are to be submitted for public scrutiny and comment before it is enacted allowing for at least one month for interested parties to comment and make proposals. Should the proposals from interested parties be rejected, a written explanation for rejecting should be provided. These laws should be made effective only after allowing market participants time to become familiar with it and take steps to implement it except in emergencies or for exigencies where two weeks grace period is allowed.

Furthermore, where an insurance supplier is applying for license, a written statement setting out information on the procedure and documents required in a simplifying and accelerating the application should be provided. There should also be established procedures for ascertaining credit worthiness of insurance companies by customers. Insurance companies should also be at liberty to provide information to independent rating organisations. Furthermore, subject to GATS provision for exemptions to protect privacy of individuals, members should ensure availability of information on financial services from domestic or foreign sources to registered insurance suppliers. Also, non-discriminatory rules and procedures governing the identification and handling of financially troubled institutions are to be publicly available. Finally, taxation measures that affect insurance should not enter into force until it has been notified WTO through a semi-annual notification process.

Solvency and Prudential Focus should be such that filing and approval shall not be required for new products or rates except for compulsory insurances. Where this is required, explanation for the policy reasons should be given and there shall be no limit on number or frequency of new products to be introduced. There should be no

restrictions on payment of dividends by foreign insurance companies provided solvency requirements are met. Members are to encourage the adoption of best practices as recognized by international standard setting organizations such as the International Actuarial Standards Association for the evaluation of the financial strength of insurance companies.

Insurance Monopolies must be prohibited from operating outside their area of monopoly designation and regulatory and supervisory measures should be put in place to prevent the monopolies from abusing their position especially in areas where competition is allowed. Where they are allowed, insurance monopolies must maintain separate accounts for monopoly and non-monopoly activities. With regards to the regulatory body, it should be an independent government entity which is impartial to all participants, and encourages a competitive insurance market.

The Model Schedule and Best Practice are good regulatory models relevant for the liberalisation of the NII and are appropriate for developing countries. First and most important is the social benefits of insurance and its relationship with economic development of developing countries. Insurance as was revealed in earlier analysis<sup>21</sup> provides unique functions separate from banks and capital markets. Therefore, the market needs to be efficient, competitive and liberalised to ensure its development and to alleviate the poverty in developing countries. Secondly, the model schedule represents the expectations and desires of foreign insurers from developed insurance markets with which developing countries need to exchange reciprocal market access

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<sup>21</sup> See discussion on role of insurance in s2.2.

and NT commitments to receive social, financial and economic benefits. It would therefore be appropriate to mould domestic reforms after this model to meet global standards and ensure the credibility of the domestic regulatory systems of developing countries. Furthermore, foreign insurers bring along their ‘experience, consumer responsive products and sales experience which will not only create greater demand for insurance products but also help in confidence boosting for the insurance industry in developing countries such as Nigeria where the public perception of insurance firms is bad<sup>22</sup>. Due to the inherent lack of capacities associated with regulatory mechanisms in developing countries, technical assistance is of utmost necessity for insurance liberalisation<sup>23</sup> and this could be gotten from the WTO/GATS, standard setting bodies like the IAIS, governments and the industry. This model and best practice is a form of assistance from industry practitioners who comprise the FLWG to complement the GATS regulatory model. Similarly, the fact that market access gains from negotiations may be lost through domestic regulatory activities necessitate the need for model regulatory best practices which helps create effective legal framework for insurance in developing countries. Domestic regulations and transparent regulatory process are both critical to the development of insurance markets<sup>24</sup>. Most importantly, the GATS is the only platform that can provide predictable rules and regulations which foreign insurers desire for protection for the long-term nature of insurance contracts<sup>25</sup>. The model schedule and best practices is fashioned after insurance commitments in the GATS and therefore relevant to the regulatory needs of Nigeria and other developing countries. The best practice is a regulatory model that ensures prudence and transparency two vital elements in an

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<sup>22</sup> Snyder (n15)759.

<sup>23</sup> *ibid* 759.

<sup>24</sup> *ibid* 760.

<sup>25</sup> *ibid* 761.

efficient and effective regulatory process. Evidently, the model schedule and best practice is relevant and applicable to Nigeria and other developing countries.

It is also pertinent to compare the insurance model schedule with other regulatory models for liberalisation in the GATS like the Telecommunications Reference Paper which contains regulatory and other feature necessary for the liberalisation of telecommunications under the GATS and the Accountancy Disciplines.

The insurance model and the Telecommunications Reference paper are similar because both were services driven by the need for good regulatory practice to complement liberalisation. They apply to a highly regulated sector which had huge government influence but needed to be well-functioning in order to form part of the economic infrastructure. Both documents have additional commitment relating to the GATS Article XVIII because it goes beyond regulatory issues such as licensing, transparency and necessity. However, the Telecommunications Reference Paper has been successful adopted<sup>26</sup> because of the need for a competitive telecommunications sector by governments most of whom previously had full monopolies in this sector<sup>27</sup>. Unlike the telecommunications reference paper, the insurance model schedule and best practices have not been generally adopted as a model for request and offers in insurance services negotiation in the GATS. This is partly as a result of failure of negotiations in the agriculture sector which has spilled over and brought about difficulties in reaching consensus in insurance negotiation and also disagreements among FWLG mainly the EU and US<sup>28</sup>. Ironically both have used the model schedule

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<sup>26</sup> Having been used by about 69 members to schedule their specific commitments at the time the Basic Agreement on Telecommunications came into force; Cooke (n12) 376.

<sup>27</sup> Cooke (n12) 375.

<sup>28</sup> Snyder (n15) 755.

as a basis for their request/offer<sup>29</sup>. The origins of both texts are not similar. The telecommunications paper was driven by the need to ‘prevent abuses of dominant market players’ or ‘de facto monopolies’ through an effective regulatory framework<sup>30</sup> while the insurance model schedule was driven by dominant players seeking market access in developing countries. Furthermore, the insurance model was drafted mainly by insurance associations in the Quad while the Telecommunications Paper received contributions from all willing delegates who joined the ‘Friends of Telecommunications’ group. Therefore, the origin of the model schedule may have affected its acceptability in no small measure.

On the other hand, the Accounting Discipline was adopted by all members of the WTO under Article VI (4) and it has the quality of universalism and commands adherence of all members. The Insurance Model Schedule is not an insurance discipline and has not been considered as one.

The IAIS is another body that provides regulatory assistance for developing countries recognised in the GATS as a standard setting body. It is a body that has helped in the convergence and harmonisation of standards between developed and developing countries<sup>31</sup>. Therefore, its principles and relevance are considered next.

#### **4.2.3 IAIS INSURANCE CORE PRINCIPLES**

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<sup>29</sup> Cooke (n12) 374.

<sup>30</sup> Thomas Cottier and Markus Krajewski, ‘What Role for Non Discrimination and Prudential Standards in International Finance Law’ (2010) 13 JIEL 817, 830.

<sup>31</sup> Snyder (n15) 758.

## Background

The IAIS is the global association of insurance supervisors established in 1994 representing insurance supervisors in about 190 jurisdictions in the world. The objectives of IAIS include cooperation amongst its member to improve supervision of insurance industry world over to ensure its efficiency and stability, to promote well regulated markets and contribute to global financial stability. This is based on the belief that a well regulated market can secure the protection of policyholder, attract and retain capital.

The IAIS and the GATS are both harmonized measures but unlike the GATS, it is a standard setting body (SSB) that works closely with a lot of international organizations especially standard setting financial bodies. They include the WTO, International Insurance Society (IIS), International Insurance Foundation (IIF), Basel Committee on Banking Supervision, UNCTAD, International Actuarial Association (IAA), International Organization of Pension Supervisor (IOPS) to mention a few. The IAIS is relevant to the GATS provisions on domestic regulations which states that a member's conformity to obligations in committed sections would take account of the international standards of relevant international organisations applied by a member<sup>32</sup>. Nigeria is a member of GATS and IAIS so therefore, if its conformity to obligations in the insurance sector becomes an issue, the standards of IAIS would be the relevant standard to be applied. Secondly the principles of IAIS are geared towards facilitating a sound insurance market which supports the liberalisation framework of WTO/GATS

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<sup>32</sup> GATS Agreement Art VI:5.

The IAIS core principles ‘provide a globally-accepted framework for the regulation of and supervision of insurance sector’ and ‘the basis for evaluating insurance legislation, and supervisory systems of procedures’<sup>33</sup>. IAIS also provides ‘training and support on issues related to insurance supervision’, and organizes meetings and seminars for insurance supervisors<sup>34</sup>.

There are twenty eight (28) core principles grouped under six (6) headings as follows:

#### **a. CONDITIONS FOR EFFECTIVE SERVICE**

Insurance supervision should rely upon a policy, institutional and legal framework, a well-developed infrastructure and an efficient financial market<sup>35</sup>. This means that the government should have an established publicly stated policy statement aimed at promoting financial stability and an institutional and legal framework comprising public institutions, laws and regulations which address issues emanating from the financial sector. This is sine qua non for the financial industry to ensure predictability and transparency. The sensitive nature of this sector is such that no aspect of this should be left to discretion. In the same vein, predictability is a very important factor in trade in financial services. Therefore, for foreign suppliers of insurance services, the total framework must be well defined and effective. There must be a legal infrastructure consisting of a well-functioning judicial system with officers trained in financial matters and are able to enforce their decision without hindrance. There is also need for the use of transparent and documented standards in accounting, auditing

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<sup>33</sup> IAIS, Introduction, Insurance Core Principles and Methodology <[http://www.iaisweb.org/ temp/Insurance\\_core\\_principles\\_and\\_methodology.pdf](http://www.iaisweb.org/temp/Insurance_core_principles_and_methodology.pdf)> accessed 9<sup>th</sup> October 2010.

<sup>34</sup> IAIS, ‘About IAIS’ <<http://www.iaisweb.org/index.cfm?pageID=28>> accessed 9th October 2010.

<sup>35</sup> IAIS Insurance Core Principle (ICP)1.

and actuary consistent with that of international standards. Finally, an efficient financial market would comprise an efficient market that supports both long and short term investments. These include a well-functioning banking, securities and money market. These are the essentials an effective service delivery of the insurance supervisory authority.

## **b. THE SUPERVISORY SYSTEM**

Supervisory Objectives must be clearly defined<sup>36</sup> and the supervisory authority must have adequate ‘powers, legal protection and financial resources’ and be ‘operationally independent and accountable’ in exercising these functions and powers. It must be able to ‘hire, train and maintain sufficient staff with professional standards<sup>37</sup>. The supervisory authority must have a legal mandate inscribed in the insurance law that sets out its publicly defined objectives which serve as benchmark for assessing the activities of the authority. It is important that the major objective should include the promotion of a stable, efficient and fair insurance market geared towards the protection of policyholders and other stake holders. The powers of the supervisory authority should be adequate in carrying out its objectives and functions without hindrance. Also, the internal governance structure of the authority should ensure its integrity and be free from governmental, political or industry interferences or influences. The powers of the supervisory authority if not defined and made independent will make the activities of the authority ineffective and this would be a hindrance to the development of the market and the economy which the insurance sector is meant to service.

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<sup>36</sup> *ibid* ICP 2.

<sup>37</sup> *ibid* ICP 3.

These functions must be carried out in a transparent and accountable<sup>38</sup> manner while sharing information with other relevant supervisory bodies<sup>39</sup> especially within the finance industry. This is because all these sectors affect each other and supervision in one would require information from the other. This underscores the need for supervisory cooperation to influence a consolidated form of supervision in the entire financial sector<sup>40</sup>.

### **c. THE SUPERVISED ENTITY**

All insurers must be licensed through a process which is clear, objective and public<sup>41</sup>. The owners, board members and management staff including actuaries and auditors must be persons fit and proper possessing not only professional qualification but must also be persons of integrity, competence and experience<sup>42</sup>. Proposals to directly or indirectly acquire ownership or interest in an insurance company must be presented to the regulatory authority for approval. Likewise, mergers and portfolio transfers must be approved by this body<sup>43</sup>. The corporate governance structure should recognize and protect the rights of all parties of interest and the supervisory authority is required to comply with this framework. It should involve corporate discipline, transparency, accountability fairness and social responsibility while the board should be the focal point of governance system<sup>44</sup>. Internal controls system must be commensurate with the scale of business and enable both board and management to monitor and control

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<sup>38</sup> *ibid* ICP 4.

<sup>39</sup> *ibid* ICP 5.

<sup>40</sup> IMF, 'Evaluating Financial Sector Supervision: Banking, Insurance and Securities Markets' in *Financial Sector Assessment: A Handbook* (World Bank, 2005) 155  
<<http://www.imf.org/external/pubs/ft/fsa/eng/pdf/ch05.pdf>> accessed 12 April 2011.

<sup>41</sup> *ibid* ICP 6.

<sup>42</sup> *ibid* ICP7.

<sup>43</sup> *ibid* ICP 8.

<sup>44</sup> *ibid* ICP 9.

the operations of the business<sup>45</sup>. Insurance companies need to be properly administered and compliance with rules and regulations is the key to protecting policyholders for whom the regulatory and supervisory infrastructure is created. However, for trade purposes, ineffective and inefficient supervision is dangerous because foreign suppliers may be difficult to control; a situation that may cause the economic conditions to become worse than before liberalisation.

#### **d. ON-GOING SUPERVISION**

This examines the surveillance mechanisms which involve the supervisory authority engaging in market analysis and through monitoring and analysing factors that affect the market, drawing conclusions and taking appropriate actions<sup>46</sup>. The supervisor must receive enough information to enable off-site monitoring and evaluation of the market and individual insurers<sup>47</sup>. It must organise on-site inspection and ascertain conformity with legislative and supervisory requirements<sup>48</sup>. Where needed, the supervisory authority should enforce corrective action<sup>49</sup> and impose publicly disclosed sanctions that are clear and objective<sup>50</sup>. However, in cases of winding up or exit of firms, a wide range of options for orderly exit from the market through legislative and supervisory means must be available. This must define solvency and procedures for dealing with it giving priority to the protection of policyholders<sup>51</sup>. Supervision should be both on solo basis and group-wide basis to ensure that insurance companies belonging to groups do not get financially destabilised by group

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<sup>45</sup> *ibid* ICP 10.

<sup>46</sup> *ibid* ICP 11

<sup>47</sup> *ibid* ICP 12.

<sup>48</sup> *ibid* ICP 13.

<sup>49</sup> *ibid* ICP 14.

<sup>50</sup> *ibid* ICP 15.

<sup>51</sup> *ibid* ICP 16.

activities<sup>52</sup>.

The supervision of insurance companies needs to be continuous ensuring strict compliance with all rules and standards including solvency provisions. There is need to sanction erring companies, without fear or favour further confirming the need for an independent supervisory authority.

Where the insurance company is part of a group, without micro and macro supervision, there may be some inherent risks within the group that would not be revealed by an assessment of the insurance company alone. This becomes more important with current trend of insurance buying into banking and banks buying into insurance companies and Securities Company. Obviously once the group is financially distressed, all the firms within the group would be affected hence the need for group-wide supervision. Finally, in situations of bankruptcy, alternative options need to be considered in the best interest of policy holders. Policyholders are faced with financial jeopardy when insurance companies collapse because the financial succour expected from purchasing insurance is lost. Therefore, insurance firms need to be supervised for effective performance. This promotes a healthy industry attractive to foreign suppliers and ensuring positive gains from a liberalised insurance market. Effective surveillance mechanisms which promote market credibility and investor confidence in insurance markets is necessary for effective liberalisation.

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<sup>52</sup> *ibid* ICP 17.

## e. PRUDENTIAL REQUIREMENTS

Insurance supervisors need to do effective risk identification, assessment and management<sup>53</sup>. Knowing insurance to be a risk taking activity it needs to ensure that insurers do risk evaluation and management through reinsurance and other tools to ensure adequacy of levels of premium<sup>54</sup>. It should require compliance of insurers to standards of technical provisions and other liabilities while the supervisory authority has authority to access the adequacy and possibly increase these provisions<sup>55</sup>. The supervisor must ensure compliance with investment standards such as investment policy, asset mix, diversification and asset-liability matching<sup>56</sup>. It should also ensure compliance with standards on the use of derivatives and similar commitments to be ensured by supervisory authority especially on restrictions and disclosure requirements as well as internal controls and monitoring<sup>57</sup>. Compliance with solvency regime including capital adequacy requirements and suitable forms of capital that would enable the insurer absorb significant losses<sup>58</sup> should also be enforced.

The need for prudential consideration has consistently emphasised in this thesis and in almost all international agreements, models and standard setting texts examined. As a risk transfer mechanism, insurance companies have a duty to do effective risk management and risk control. There are various mechanisms for risk control that insurance companies can employ but the supervisory authority should ensure that the risk management of insurers is commensurate with the level of business risks underwritten. This underscores the need for risk-based regulations and supervision in

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<sup>53</sup> *ibid* ICP 18.

<sup>54</sup> *ibid* ICP 19.

<sup>55</sup> *ibid* ICP 20.

<sup>56</sup> *ibid* ICP 21.

<sup>57</sup> *ibid* ICP 22.

<sup>58</sup> *ibid* ICP 23.

insurance<sup>59</sup>. The level of internal control is also a function of risk management analysis, assessment and control. It is therefore imperative that the supervisory authority has adequate manpower to ensure that proper risk management is done by insurance companies, and standards which have been publicly declared in the regulatory policy and legal framework are strictly enforced. Regulatory efficiency and effectiveness promotes effective liberalisation and maintains a healthy market with the prudential regulations and supervision.

#### **f. MARKET AND CONSUMERS**

The requirements for the conduct of business by intermediaries must be set by supervisory authority directly or through the supervision of insurers<sup>60</sup>. It should set minimum requirements for insurers and intermediaries in dealing with consumers including foreign insurers selling products on cross-border basis. This should include timely, complete and relevant information before a contract of insurance is concluded<sup>61</sup>. The supervisory authority is to make insurers disclose timely and relevant information that gives a clear view to stakeholders about the financial status of their business and an understanding of the risks which they are exposed to<sup>62</sup>. It should also maintain that insurers take measures that prevent, detect and remedy insurance fraud<sup>63</sup>. The supervisory authority should make sure all life and investment related insurers take measures to deter, detect and report money laundering and financing of terrorism in line with the recommendations of the Financial Action Task

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<sup>59</sup> See discussion in s2.4.

<sup>60</sup> *ibid* ICP 24.

<sup>61</sup> *ibid* ICP 25.

<sup>62</sup> *ibid* ICP 26.

<sup>63</sup> *ibid* ICP 27.

Force on Money Laundering (FATF)<sup>64</sup>.

These principles are geared towards consumer protection and insurance market stability. Therefore, it is important that the insurance supervisory authority set a minimum level of care for consumers. It is equally imperative that relevant information is publicly available to assist the consumer in making rational decisions about insurance policies. This is imperative since insurance contracts come in small prints, and are often difficult to comprehend. Consequently, small prints have been outlawed in some countries<sup>65</sup>. Likewise, the integrity of the market determines the level of investment it attracts from foreign investors. Without a system of transparency where company information is publicly available, and surveillance structure that easily detects sources of risk, liberalisation would not yield positive results. This is because the domestic market is often an unfamiliar terrain for foreign suppliers of insurance and non-availability of this information would therefore become a hindrance to investment in the respective market.

#### **4.2.4. MARKET ACCESS AND INSURANCE IN THE CURRENT GATS NEGOTIATIONS**

Market access in insurance has been challenging with huge regulatory limitations and restrictions in place in many jurisdictions. Like other financial services regulators insurance regulators have a lot of freedom under the AFS prudential carve out<sup>66</sup> which result in the application of laws and regulation that may not promote competition. Consequently, foreign suppliers often find that market access gained in negotiations get lost in the application of non-competitive and non-transparent prudential

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<sup>64</sup> *ibid* ICP 28.

<sup>65</sup> Such as the EU and US.

<sup>66</sup> See discussion in s4.1b above.

regulations. Domestic regulations are therefore very crucial to the development of insurance markets.

Market access for cross border trade in insurance is prohibited in many jurisdictions and there is a general restriction on entries of professional service suppliers in the entry of natural persons mode of trade. Cross border trade in reinsurance is highly restricted with most regulations having a mandatory necessity test in place. The commercial presence mode is the most favoured form of market access though a number of regulatory restrictions are associated with it. These include restrictions on the juridical nature of branches or on the forms of establishment including foreign equity caps<sup>67</sup>. Regulations sometimes reserve certain insurance products for domestic firms thereby making foreign insurers unable to participate in such businesses. For example in Nigeria the law requires that all imports to be insured by domestic insurance firms and series of approval needs to be obtained before cross border purchase of reinsurance services can be made.

Negotiations in insurance services have also been quite disappointing in the current GATS rounds of negotiations because of the inadequacy in the quantity and quality of offers made. It is said that the problems in the agricultural services negotiations has undermined negotiations in trade in services including insurance<sup>68</sup>.

Commitments in insurance services are still skewed in favour of commercial presence with only a few instances of full commitments. Many members still maintain their limitations on 'the entry of insurance providers'. The commonly found limitations

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<sup>67</sup> Evans (n13) 745,

<sup>68</sup> Snyder (n15) 756.

persist in foreign equity and restrictions on foreign branching. Other limitations relate to legal entity and quotas on the number of suppliers. In reinsurance services often a necessity test applies and there is also a practice of reserving some classes of insurance usually compulsory for domestic insurance firms.

Out of 69 offers submitted in Doha, only about 30 contain improvement either by addition of new subsectors or improving on existing commitments. Apart from developed countries, only accession countries have made deeper commitments in the current round of negotiations. However, 'further and deeper commitments have been sought specifically in cross-border trade in insurance'<sup>69</sup>.

There seems to be no 'flexibility to remove foreign equity caps, juridical form restrictions, quantitative/numerical restrictions, or economic needs test requirements'<sup>70</sup>. Only a few offers have been received relating to 'the cross-border supply of reinsurance and large-scale commercial risk insurance services'<sup>71</sup>. Co-sponsors believed that offers from recipients were in need of substantial improvement to achieve the request's liberalisation objectives. Offers generally are minimal and short of level of liberalisation already existing in member countries. Nigeria has made no offers in the current round though it had received requests from EU on horizontal commitments and reinsurance necessity test<sup>72</sup>.

The failure of negotiations in WTO has resulted in a proliferation of bilateral

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<sup>69</sup> Cooke (n12) 400.

<sup>70</sup> WTO, 'Negotiations on Trade in Services' Report by the Chairman to the Trade Negotiations Committee, (2011) TN/S/36' para 32.

<sup>71</sup> *ibid.*

<sup>72</sup> See discussion on specific commitments in s3.2.2.

agreements prominent amongst them are the United States free trade agreements with countries such as Korea, Chile, Singapore etc<sup>73</sup>. This move had given the general impression that WTO was irrelevant. However, experiences from these bilateral agreements has revealed that the long term predictability and certainty which foreign suppliers of insurance services require of domestic regulations and measures can only be achieved under the multilateral platform of the WTO/GATS<sup>74</sup>. This confirms the fact that commitments in this framework are of better value than what obtains in bilateral or unilateral liberalisation arrangements.

The analysis in the first part of the chapter has addressed the structure and liberalisation framework of GATS which includes the GATS Agreement, AFS along with the insurance models, best practices and ICPs provide frameworks for liberalisation of insurance services. The first two have the force of law and are binding but the last two though are persuasive in nature represent well recognized standards for insurance liberalisation within GATS. It also examined the effect of regulations on market access and the current state of negotiations in insurance.

From the analysis this thesis reveals first, that GATS is a viable model for liberalisation and secondly a paradigm for testing NII liberalisation can be derived. These are necessary conditions expected by foreign insurance providers from liberalised insurance markets like Nigeria that can facilitate mutually beneficial multilateral ties. This paradigm is discussed in the second part of this chapter below.

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<sup>73</sup> *ibid* 757.

<sup>74</sup> *ibid* 761.

## **PART B**

### **4.3 PARAMETERS FOR INSURANCE MARKET LIBERALISATION**

These parameters were derived from the analysis in chapters two, three and part ‘A’ of four. The parameters include mainly factors that support a successful liberalisation of insurance services in the WTO/GATS liberalisation framework. This is the preferred model for liberalisation and its principle and rule based structure provides regulatory models upon which reforms can be based. However, this platform does not prescribe standards rather it gives members regulatory autonomy. The parameters therefore used models deriving from the GATS framework together with globally recognised standards that would complement and enhance the potentials for growth in the WTO/GATS model.

#### **4.3.1 LEGISLATIVE PARAMETERS**

The parameters relate to the legal framework of the insurance sector and form the basis of the legislative aspects of the model of reforms. It mainly involves the removal of restrictions to market participation, adoption of principles-based regulations and risk based prudential regimes.

##### **Removal of Restrictions on Market Participation**

This parameter is derived mainly from the Insurance Model and Best Practices. Here, market access is desired in all modes of supply in trade in services. For cross border modes, the desire is mainly for reinsurance and transportation classes of insurance like marine and aviation. In reinsurance the removal of practices of compulsory

cession and right of first refusal is required. The same view is held on transportation insurance laws that give domestic suppliers exclusive rights.

For commercial presence mode, the removal of laws prescribing maximum equity shareholding for foreigners or allowing monopolies and exclusive providers is required. Likewise the ability of a foreign supplier to set up a new company or acquire an existing company as a branch in the host country is included. The method of participation could also be by joint venture and the percentage of equity shareholding of the foreign supplier should be determined solely by the parties. Foreign equity share restrictions should also be eliminated over a period of two years.

Furthermore, it is also anticipated that regulations recognise the relationship between the parent company and new company. The foreign supplier must be able to provide services in the host market using its home company name provided it does if existing trademarks is not infringed. It should not be denied access on the basis of its legal nature at home. Regulations should remove restrictions on participation in compulsory insurances, insurances of state owned enterprises and also on pensions management.

Additionally, in the temporary entry of natural persons mode, the need is for prompt visa provisions for professionals wishing to enter temporarily for the purpose of supplying their services such as brokers, consultants and most importantly, international claim and average adjusters. Nationality should be avoided when foreign

suppliers maintaining a commercial presence choose resident representatives in the host country. All that is important is that the representative meets regulatory competency requirements. Besides, the provision of temporary visas should be timely for professionals employed by foreign suppliers.

### **Adoption of Principle Based Regulations**

This parameter is derived mainly from GATS Article VI which attempts to control the regulatory prerogatives of members so that regulations are not used as barriers for trade. This parameters test for fairness and objectivity of laws especially as it affects foreign suppliers of insurance services. The desires here are for the adoption of regulatory principles such as reasonableness, proportionality, remedial procedure, prompt-authorization, transparency, and international standards in the regulatory framework. Licensing conditions should also be fast and not burdensome or trade restricting.

### **Adoption of Risk Based Regimes**

This involves the adoption of and prudential regulations which include risk based capital requirements and solvency regimes. This parameter was constructed from the synchronization of the prudential carve-out in the AFS and the conceptual analysis of insurance presented in chapter two. It is premised on the fact that inadequate and ineffective regulations are at the roots of calamitous results in the liberalisation process.

## **4.3.2 INSTITUTIONAL PARAMETERS**

The institutional parameters derive mainly from the analysis of the IAIS ICPs which

is the globally recognized standard for insurance regulation and the conceptual analysis of in chapter two. There are three main institutional parameters.

### **Supervisory Objectives**

The requirement is a well-defined objective that would promote efficient, clear and safe market for the policyholders. The goal of supervision is protection of the policyholders.

### **Supervisory authority**

The supervisory authority should have powers, resources and be independence and accountability.

**Powers** -the supervisory authority should have adequate power to take immediate action to achieve its objectives, especially to protect policyholders' interests

**Resources-** i.e. budget, infrastructure and tools sufficient for effective supervision, to attract and retain skilled staff, hire experts when necessary and provide training for staff. It should have staff with appropriate levels of skills and experience. These staff must have necessary legal protection while discharging their duties.

**Independence and Accountability** - proper governance structure including internal audit of the Commission; clear procedures for appointment and removal of members of the governing board and public disclosure of removal and

rational for it, clearly defined relationship mechanism between the agency and the government and ensuring freedom of the supervisory agency from any form of influence; clearly defined funding structure that does not undermine the independence and freedom of the agency to allocate its resources. Furthermore, independence and accountability requires the representatives of the supervisory authority to publicly explain its objectives and report to the public its activities and performance in achieving the objectives.

### **Supervisory process- Transparency, Cooperation and Surveillance**

The authority should conduct its functions with public knowledge and consultations on the supervisory process. Proposed and existing regulations should be available for public scrutiny. It must publish audited financial statements on a regular basis. It should also cooperate with other relevant regulators especially for the purpose of internationally active insurers. Finally, in the institutional model of reforms, there are surveillance structures in place in form of on-site, off-site and on-going supervision. The supervision is risk based and frequency of on-site supervision is dependent on the risk profile of individual firms and results of off-site analysis of submitted reports. In-depth market qualitative and quantitative analysis is done to identify the risk and vulnerability of the so that prompt intervention will reduce chance of future problems. The agency therefore engages in both preventive and corrective measures to ensure an efficient and competitive market. The agency's analysis however involves not only internal domestic but also international trends which may impact the market.

These legislative and institutional parameters would be used as indices for the extent of liberalisation of the NII.

#### 4.4 CONCLUSION

This chapter reviewed the liberalisation platform for insurance under the GATS together with other international models deriving from it and argues that the framework is flexible allowing for progressive liberalisation and assistance to developing countries. Market access and current negotiations in insurance were also examined and it was revealed that the request and offers in insurance was very minimal and restrictions were predominant in developing countries. The proliferation of bilateral agreements was also noted. However, as argued in earlier chapters, the benefits and credibility of reforms in the NII can only be accentuated with locked in commitments in the GATS. This thesis argues that developing countries stand to benefit more from multilateral negotiations based on the lessons learnt from Doha and earlier analysis about the interference of bilateral agreements with non-economic issues amongst others.

The legal analysis continues in the next chapter which reviews legislation in the NII *vis a vis* the legislative model of reforms for insurance liberalisation constructed in this chapter. This is to ascertain through legal analysis the laws that were in compliance and those requiring change.

## **CHAPTER FIVE**

### **THE NII LEGAL FRAMEWORK AND THE LEGISLATIVE MODEL OF LIBERALISATION**

#### **5. INTRODUCTION**

The last chapter reviewed the liberalisation framework of the GATS for insurance and other models deriving from the platform. It also analysed the IAIS core principles together with market access and current negotiations in GATS on insurance and concluded with the construction of two sets of parameters necessary for the liberalisation of insurance using the WTO/GATS framework. These form the model of reforms being proposed for the NII. The first set of parameters are legislative in nature while the second relates to the institutional aspects of insurance i.e. administration and supervision. This chapter reviews the legislative framework of NII against this model of legislative reforms for liberalisation.

The analysis is divided into six sections with the first presenting the model of legislative reforms while the second gives a brief overview of the laws forming the legislative landscape of the NII. The third section examines measures not compliant with Nigeria's commitments in the GATS which need to be changed. The measures that comply with Nigeria's GATS commitment but are not sufficiently liberal are examined in the fourth section while the fifth section reviews measures which not only comply with GATS but also support liberalisation. The last section contains conclusions on the chapter.

## 5.1 THE MODEL OF LEGISLATIVE REFORM FOR THE NII

The legislative model proposed for reforms in the NII involves three main aspects which are the removal of restrictions on market participation, the adoption of principle-based regulations and risk based regimes. It entails polycentric PBR<sup>1</sup> which are in compliance with GATS general obligations and its provisions on domestic regulations<sup>2</sup> such as fairness and objectivity of laws. The laws and measures particularly those relating to foreign participation are streamlined to make it easier and clearer to understand and comply with. Regulatory principles such as reasonableness, proportionality, remedial procedure, prompt-authorization, transparency, and international standards are enshrined in the regulatory framework for prompt processing of licenses. The legislations are pro-competition they are therefore not burdensome or trade restricting.

This model also consists of risk based regimes such as prudential regulations, risk based capital requirements and solvency regimes which focuses on enterprise risk portfolios. There are no generally prescribed capital or solvency requirements rather prudential regimes are based on the individual risk assessment of each firm.

Market access is encouraged in all modes of supply in trade in services. In cross border modes, reinsurance services trade is devoid of practices of compulsory cession, right of first refusal, localization of assets or collateralization for foreign reinsurance suppliers. The laws relating to transportation classes of insurance do not give

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<sup>1</sup> See discussion on principled based regulations in s2.4

<sup>2</sup> The General Agreement on Trade in Services Art VI.

domestic suppliers exclusive rights.

For commercial presence mode, there are no laws prescribing maximum equity shareholding for foreigners or allowing monopolies and exclusive providers. Foreign suppliers are able to set up new companies or acquire existing ones as branch in the host country. The modes of participation allowed include joint ventures and the percentage of equity shareholding of the foreign supplier would be determined solely by the parties. Foreign equity share restrictions would be eliminated where necessary over a transition period not exceeding two years.

Under this legislative model, regulations recognise relationships between parent companies and new companies while foreign suppliers are allowed to provide their services using their home company name when not infringing on existing trademarks. Foreign suppliers are not denied access due to their legal nature at home. There are also no legal restrictions on the participation of foreign suppliers in compulsory insurances, insurances of state owned enterprises or in pension management. Foreign suppliers are at liberty to choose representatives in the host country irrespective of their nationality when the representative meets regulatory competency requirements. Regulations guarantee timely and transparent processing of temporary visas for foreign professionals employed by foreign suppliers and those in the temporary entry of natural persons mode such as brokers, consultants and international claim and average adjusters.

## **5.2 THE NII LEGISLATIVE LANDSCAPE**

The substantive laws in the NII as earlier noted are the I A 2003 and NAICOM

Guidelines and Code respectively while other laws affecting the NII include Companies and Allied Matters Act of 2004; Nigerian Investment Promotion Commission Act of 2004; Immigration Act of Cap 171 of 1990; Securities and Exchange Commission Acts of 1988, 1999 and 2007; and the Foreign Exchange (Monitoring and Miscellaneous Provisions Act of 2004 which are analysed below.

### **INSURANCE ACT (IA) OF 2003**

This is the main insurance legislation passed into law on the 27<sup>th</sup> of May 2003 specifically regulating the NII. The Act contains 102 sections divided into 14 parts covering regulatory subjects such as application of the Act, registration of insurance minimum share capital, modes of operation of insurers and the administration of the Act to mention a few. Though some principles could be implied into some provisions, there is no specific reference to principles as it relates to GATS in the IA which is the substantive law in the legal framework of the NII. The Act is mainly performance based and contains no risk based regimes in its prudential provisions. NAICOM the regulatory agency of government for insurance is empowered to administer and enforce the Act.

### **NAICOM GUIDELINES, DIRECTIVE AND CODES**

NAICOM the NII supervisory authority is empowered to issue guidelines for insurance institutions<sup>3</sup> who are obliged to comply with.<sup>4</sup> The Commission has actively employed this power in complementing the provisions of the IA 2003 through the issuance of annual guidelines, codes of conduct and directives since 2006 and this has

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<sup>3</sup> National Insurance Commission Act of 1997 s49 (1) (b).

<sup>4</sup> *ibid* s49 (5), Failure to comply with guidelines attracts a fine or prison sentence.

contributed immensely to the legal framework of the sector.

NAICOM's directives provide prudential regulations relating mainly to solvency requirements, financial reporting, technical requirements like reserves and human capital requirements. Like the IA 2003, all the NAICOM rules are performance based and not risk based. The solvency regulations of NAICOM encompass all the necessary criteria as defined by international standards such as the IAIS<sup>5</sup>. It addresses issues of valuation of liabilities and assets including the quality and liquidity of such assets. It defines suitable forms of capital and capital adequacy requirements. NAICOM directives also provide practical interpretations to IA 2003 provisions on the calculation of admissible and non-admissible assets in its annual guidelines. However, none support risk based regimes.

### **COMPANIES AND ALLIED MATTERS ACT OF 2004 (CAMA)**

This is the cardinal law on business in Nigeria<sup>6</sup>. CAMA is administered by the Corporate Affairs Commission (CAC)<sup>7</sup> and governs the incorporation, operation and ownership of both private and public companies in Nigeria<sup>8</sup>. It is broken into three parts with regulations on incorporation of companies forming Part A, Incorporated Trustees in Part B while Part C deals with schedules. CAMA has implications for the NII with regards to form, registration and incorporation of insurance companies. It also makes provisions for the incorporation of foreign companies. CAMA was fashioned after the British Company's Act of 1948 with some minor alterations but it has remained in its original form since enacted in 1990.

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<sup>5</sup> Insurance Core Principles (ICPs) 23

<sup>6</sup> The IA 2003 s3 (a) and s100 make CAMA supplementary to the Act.

<sup>7</sup> The CAC is a body corporate established under CAMA for the administration of the Act.

<sup>8</sup> S21(2) and 22 of CAMA provides that a private company should not have more than 50 members while a public company is any company with above 50 members, A foreign insurer may acquire shares in any convertible foreign currency and its investment dividends can be repatriated freely.

## **THE NIGERIAN INVESTMENT PROMOTION COMMISSION ACT (NIPC) 2004**

This is the law establishing the Nigerian Investment Promotion Commission, a federal government agency charged with encouraging, promoting and coordinating investment in Nigeria<sup>9</sup>. The NIPC initiates and supports measures to enhance investment, collate and disseminate information on investment opportunities and maintain liaison between investors and ministries, government departments and agencies concerned with investment<sup>10</sup>. Therefore, as the investment authority in Nigeria it has a dual role in foreign investment and its regulation. It makes laws aimed at attracting foreign investments into Nigerian and assist foreign companies in processing their applications through various government agencies involved in the registration of the businesses they are investing.

## **IMMIGRATION ACT CAP 171 OF 1990**

This Act controls the entry and exit of persons in Nigeria and it is administered by the by Director of Immigration<sup>11</sup> under the direction of the minister charged with immigration affairs which is usually the Minister for Internal Affairs.

The Immigration Act is of significance to the commercial presence and temporary entry of persons mode of market access in the legislative parameter. It is the law under which foreign staff of incorporated foreign insurance service providers or foreign professionals seeking temporary entry to supply service gets entry visas.

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<sup>9</sup> NIPC Act 2004 s4

<sup>10</sup> ibid (b), (d), (h).

<sup>11</sup> Immigration Act 1990 s5.

## **FOREIGN EXCHANGE (MONITORING AND MISCELLANEOUS PROVISIONS) (FOREX) ACT 2004**

This is the Act that established the Autonomous Foreign Exchange Market (AFEM) where transactions in foreign exchange take place. The Act is important with regards to the commercial presence mode. It contains provisions for the importation and exportation of foreign exchange<sup>12</sup>, the operation of foreign currency domiciliary account<sup>13</sup> and payments for exports of goods and services permitted in Nigeria<sup>14</sup>. The Forex Act is also significant in the removal of restrictions on market

### **5.3 MEASURES NOT COMPLIANT WITH MODEL OF REFORMS**

The GATS deals not only with laws and regulations but on measures affecting trade in services. These measures could be either from government authorities or non-government bodies or even agencies with delegated authority like NAICOM<sup>15</sup>. This section examines regulatory measures in the NII that affects insurance services are neither compliant with Nigeria's obligations in the GATS nor with the model of reforms and therefore needs to be changed.

First, only limited liability companies are licensed to supply insurance services, a clear violation of the GATS provision on limitations. While every member has the autonomy to decide the licensing requirements, limitations in forms of specific type of

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<sup>12</sup> *ibid* s12-15.

<sup>13</sup> *ibid* s17-25.

<sup>14</sup> *ibid* s27.

<sup>15</sup> See discussion on measures affecting trade in services in chapter 4.

legal entity is prohibited<sup>16</sup>. Secondly, there is a silent embargo<sup>17</sup> on the licensing of new insurance companies which implies that anyone interested in registering an insurance company at this moment would not be successful. This policy is not made public nor is it written in any law, regulation or directive. It negates the principle of transparency a general commitment in the GATS that requires public knowledge of all measures relating to services trade. Whilst the GATS respects members' regulatory autonomy, placing secret embargos on entry of new firms breaches Nigeria's general obligations in the GATS and also restricts liberalisation. Nigeria does not have such limitations inscribed in its schedule of commitment thus this is clearly a breach of its commitment. It is also a contradiction for the market to be open in theory but not in practice. The argument is that other forms of market participation could be employed such as buying into the equity of existing insurance companies. This again negates obligations under GATS specific commitment. This is because 'measures which restrict or require specific types of legal entity or joint venture through which a service supplier may supply a service' is not allowed in sectors where Nigeria has committed such as insurance. This embargo therefore is in breach of Nigeria's specific and general commitments in the GATS. The GATS model is pro liberalisation and the embargo would need to be lifted since freedom of entry and exit from the market is also a necessary condition for competitive insurance markets<sup>18</sup>.

There is also mandatory application for a Letter or Attestation/Certificate to Reinsure Abroad (LOA/CRA) or, Approval-in-Principle to Reinsure Abroad as the case may be before cross-border reinsurance transactions<sup>19</sup>. First, an Approval-in-principle is

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<sup>16</sup> The General Agreement on Trade in Services Art XVI (2) (e).

<sup>17</sup> This information was obtained from the exploratory survey; see discussion in chapter 7.

<sup>18</sup> See chapter two for discussion on conditions of viable insurance markets.

<sup>19</sup> NAICOM s29.5 (1) and (2).

required to find reinsurers abroad and then a Certificate or Attestation is required to confirm risks that have been placed abroad. There is necessity test before issuing both letters. The Commission must be convinced that the cover sought abroad cannot be provided by local reinsurers. This provision is not only restrictive and protectionist in nature, it is also inconsistent with liberalisation of the NII. Furthermore, it is also a violation of Nigeria's obligation under the GATS Agreement because the country's schedule of commitments under market access and national treatment in reinsurance services has no restrictions inscribed on it<sup>20</sup>.

Considering the fact that efficient management of large risks requires an open market for reinsurance<sup>21</sup>, these restrictions would only constrict the underwriting capacity of the NII and make it less competitive and inefficient. Nigeria's claim of opening up her financial sector is invalidated by these protectionist policies that have negative impact on trade in services. This trade restricting measure therefore not only contravenes Nigeria's specific commitments in the GATS but also does not support liberalisation.

The regulatory process involved in issuing guidelines is not transparent and they are not publicly available again a violation of general commitment. Consequently, this restriction needs to be expunged from the legal framework of the NII.

Furthermore, the GATS expect regulations to follow international standards<sup>22</sup> but the financial reporting system of Nigeria follows no recognised standard and this presents a problem of assessment for the public because of the opaqueness of financial

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<sup>20</sup> See discussion of Nigeria's commitment in the GATS in chapter one.

<sup>21</sup> SwissRe, 'The Essential Guide to Reinsurance' (SwissRe Publications, 2010) 40.

<sup>22</sup> GATS Art VI (5)(b).

statements of insurance companies in the NII. This accounts for the poor performance and difficulty in placing appropriate value on insurance stocks<sup>23</sup> in Nigeria. Investors have difficulty assessing and interpreting insurance companies' financial reports and are therefore unable to invest in the sector.

However, with the NAICOM directive on International Financial Reporting Standard (IFRS)<sup>24</sup>, financial reporting in the NII is expected to adopt a recognised standard soon and become not only accessible and assessable.

The next section reviews measures which do not contravene Nigeria's obligations in the GATS but are not sufficiently liberal for the GATS model being proposed.

#### **5.4 LAWS COMPLIANT BUT NOT LIBERAL**

Though the GATS allow members regulatory autonomy in the enactment of laws, standard and setting conditions for domestic participation, such laws are required to be objective, fair and impartial while licensing procedure expected to be unburdensome and not trade restrictive<sup>25</sup>. In the legislative framework of the NII, some provisions dealing with registration and licensing in the commercial presence mode and market participation in other modes are compliant with GATS model of reform but not sufficiently liberalised as discussed below.

In the NII, there are five (5) major requirements fragmented under five different legislations that a foreign supplier must comply with to maintain commercial

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<sup>23</sup> Anthony Osae-Brown, 'Insurance: A Beleaguered Sector and Less than Penny Stocks' *Businessday* (Lagos, 6<sup>th</sup> June 2011).

<sup>24</sup> See discussion on IFRS in s5.5.

<sup>25</sup> The General Agreement on Trade in Services Art VI; see also discussion s3.2.2. (c).

presence. These include incorporation and three tedious registration processes under CAMA, NIPC and NAICOM, obtaining business and other permits, and importation of capital as analysed below.

All Companies including foreign suppliers of insurance services needs to obtain local incorporation and registration of the Nigerian branch or subsidiary of its organization<sup>26</sup> as a limited liability company<sup>27</sup> except exempted under the law<sup>28</sup> with the Corporate Affairs Commission (CAC). This company could have 100% foreign equity<sup>29</sup>, be a private company of less than 50members or a public company of 50 or more members<sup>30</sup>. It must have the minimum capital requirement of N2billion for non-life insurance companies, N3billion for life insurance companies, N5billion for composite insurance companies and N10billion for reinsurance companies<sup>31</sup>. The foreign subsidiary can maintain its parents name as long as it meets with the requirements of CAMA<sup>32</sup>. More important to the NII, is that the name must reflect that it is a limited liability insurance firm and it must not infringe on trademark law.

The foreign supplier also has the option of buying into or completely taking over an

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<sup>26</sup> CAMA s54 (1); NIPC ACT s19.

<sup>27</sup> The I A 2003 requires registration as limited liability.

<sup>28</sup> CAMA s54 (1), s56 and s3 IA; The companies exempted are mainly those that had been invited by the federal government to executed special projects or companies owned by foreign governments to assist in export promotions in Nigeria.

<sup>29</sup> There is no restriction on foreign suppliers' equity shareholding. CAMA only requires two people that do not fall within prohibited persons under s20 e.g. persons under 18yrs, unsound mind, bankrupt or disqualified as director under s254 of the Act.

<sup>30</sup> CAMA s22(2).

<sup>31</sup> Ordinarily, the minimum share capital under CAMA is N10,000 and N500,000 for private and public companies respectively but the IA 2003 s100 provides that in the event of inconsistency in the provisions of CAMA with regards to registration of insurance companies, the provisions of I A 2003 shall prevail to the extent of the inconsistency. Therefore, insurance companies require a different capital requirement that is consistent with the IA 2003 and this is Federal Government Directive on insurance companies' minimum capital requirement of 2005.

<sup>32</sup> CAMA s29 & 30 provides names proposed for registration must not be identical to that of an already registered company, it must reflect the its nature.

existing insurance company. In this case, it would have to fulfil the requirements of ISA and IA 2003 under Mergers and Takeovers<sup>33</sup> and not incorporation. The foreign supplier may need to register new name, Memorandums and Articles of Association under CAMA as required<sup>34</sup>. Upon completing the incorporation exercise with the CAC, foreign suppliers have to register with the NIPC taking along incorporation or other relevant documents and details of key officers of the company<sup>35</sup>.

Obtaining of and other permits is the next step in the licensing process. The Immigration Act requires a foreigner seeking employment in Nigeria either for long or short term to obtain the consent of the Comptroller General of Immigration. For temporary entry of natural persons, a Temporary Work Permit (TWP) is required while for the local branch of a foreign supplier employing foreign personnel, a business permit together with other requisite licenses such as Expatriate Quota needs to be obtained beforehand from the Nigerian Immigration Service. This expatriate quota forms the basis of 'Subject to Regularization' (STR) visa provision for foreign staff employed.

Expatriate Quota signifies the number of foreign personnel a foreign insurance service provider is allowed to employ in Nigeria and this is dependent on the level of investment in the foreign branch in Nigeria. Requirements include lease agreements, certificate of incorporation and tax clearance certificates amongst others. This is a trade restrictive measure on market participation and an extra burden the foreign supplier has to bear because it limits the number of foreign personnel employable by

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<sup>33</sup> ISA 1999 s8(1); SEC is charged with the responsibility of reviewing, approving and regulating mergers and acquisitions within Nigeria. SEC Rules and Regulations stipulate the procedures for this.

<sup>34</sup> CAMA s31 for change of name and s44-9 for alterations of Memorandums and Articles.

<sup>35</sup> NIPC Act s20.

foreign insurance providers since it is a measure not based on competence.

Apart from these restrictive entry conditions, there are also extra conditions to be fulfilled for expatriate quota renewal by the foreign supplier. First, it is mandatory that Nigerian staff understudy the foreign staff with the purpose of eventually taking over the positions of expatriates. It is required that evidence of this is submitted a before expatriate quota is renewed. Other renewal requirements include details of training programme for Nigerians and list of Nigerian senior management staff and their conditions of service.<sup>36</sup>.

This appears to be attempts at tampering with the internal administration of foreign companies which by law have juridical rights to hire, retain or fire. The goal of this provision appears to be skill transfer which was very important at the time of the enactment of this law in the 1960's. This is a very aggressive law that does not fit into the frame of things in twenty first century. Currently, skills can be transferred in more subtle ways than this Act provides. Though the GATS allow qualification requirements, it requires them to be objective and based on competence and ability to supply service<sup>37</sup>. The understudying of an expatriate falls short of the objectivity requirement of impersonality under the principled-based regulations. Considering the fact that Nigerian labour law does not encourage forcing staff on employer, this is discriminatory against the foreign company because indigenous firms are not saddled with extra requirement of compulsory training of indigenous staff or understudying of professionals. Requiring equal opportunities for all staff to progress along

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<sup>36</sup> Nigerian Immigration Website <<https://portal.immigration.gov.ng/?p=about> > accessed 13<sup>th</sup> April 2011.

<sup>37</sup> *ibid* Article VI (4)(a).

management cadre would have been a more objective alternative policy than the compulsory understudying of an expatriate. The law is biased and simply not considerate of foreign investors' interest and it is a formal form of discrimination. The Immigration Act needs to be reformed in a way to create a balance between the interests of foreign firms and those of those of the country. Expatriate staff would be needed in key positions to ensure the standard which the foreign supplier requires. A lot of foreign owned companies in Nigeria have indigenous staff in executive management positions without having to understudy anyone. What is emphasised is equal opportunities and competency.

Furthermore, there are no objective standards provided in the Immigration Act upon which decisions on Expatriate Quotas are based thereby leaving it to the discretion of immigration officials. It has negative effects also on transparency. The aim of transparency is to reduce incidences of administrative discretion. This leads one to the decision that the immigration act is obsolete<sup>38</sup>, inadequate, intrusive, discriminatory and restrictive for insurance services liberalisation.

Licensing and registration with NAICOM is the final step<sup>39</sup> in the process for a foreign insurance service provider wishing to establish presence in Nigeria<sup>40</sup>. There are twenty (20)<sup>41</sup> requirements for registration with NAICOM applying equally to both domestic and foreign suppliers. These include a filled and signed application form and receipt of payment of registration fee. Other requirements include the certificate of incorporation, memorandum and articles of association which establish

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<sup>38</sup> It has been enacted since 1963 with no amendments.

<sup>39</sup> There is the importation of capital step which is discussed under s5.4.

<sup>40</sup> This is under the IA of 2003 and the NAICOM Decree of 1997.

<sup>41</sup> These are all contained in the Insurance Act of 2003 s6(1).

the nature of the company and the fact that it is registered to provide insurance services. Particulars of directors and forms for allotment of shares which establishes good corporate governance such as the suitability of the owners of the business is also required for licensing. Other qualification requirements relate to business plan<sup>42</sup>, feasibility<sup>43</sup> and evidence of qualified staff<sup>44</sup> that establishes adequacy of the competence and skills of the proposing supplier. In addition, the foreign supplier would also be required to furnish a certificate of mandatory statutory deposit to CBN and declaration on the location of the principal or registered office of the company<sup>45</sup>.

Similarly, in respect of applicants proposing to carry on life insurance business, there are additional requirements of a signed statement by an actuary and statement on method of distributing profits between policy holders and shareholders.<sup>46</sup> However, for one proposing a reinsurance company a satisfactory business plan together with evidence of an effective treaty and retrocession.

All the above qualification requirements are all related to the functioning of a healthy insurance firm. They are objective and clear and necessary for establishing general competence. They appear like simple business requirements but when one considers the implications from the point of view of the foreign supplier, there are some burdensome aspects of the qualification requirements. For example, the proposing company is expected to have a full function office with requisite staff in place even

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<sup>42</sup> This includes a copy of the table of premium rates and their basis, standard proposal and policy forms of each class of insurance business proposed the applicant.

<sup>43</sup> This is the feasibility study of the insurance business to be transacted within the next five years.

<sup>44</sup> A staff list containing the name, qualifications, experience and address of each of the proposed Heads of Departments and Executive Directors of the applicant and evidence of expertise including formal practical training in that category of insurance business.

<sup>45</sup> *ibid* subsection (d).

<sup>46</sup> This relates to the calculation of premium rates and non-forfeiture values, advantages, terms and conditions proposed to be offered by the life assurer

before it is licensed. This is notwithstanding the fact that there is a possibility of the application being rejected; an enormous gamble the foreign supplier of service is expected to take. This is very unfavourable and does not provide a level playing field between domestic and foreign applicants. The IA needs to have provisions specifically designed for foreign insurance firms which will help determine their competence, skills and ability to provide insurance services while not occasioning unnecessary hardship on applicants. Current qualification requirements for licensing in the IA have elements of substantive unreasonableness.

The NT provisions in the GATS recognise that formally identical treatment may tilt competition in favour of domestic providers<sup>47</sup>. Though licensing laws apply equally to foreign and indigenous firms, the requirements are burdensome to foreign suppliers of insurance services. The NII legal framework for licensing is legitimate and forms part of the prudential regulations of insurance but nonetheless it is quite unfavourable to foreign providers bearing in mind the fact that there about five giant hurdles the foreign service-provider needs to cross to get licensed. This would have required the foreign supplier investing huge sums in meeting registration requirements while facing the possibility of not being granted the license ultimately. This process is highly unreasonable and may be the reason why foreign investment in the insurance sector has only been in existing insurance firms rather than setting up a subsidiary. Streamlining the process would better enhance the liberalisation of the NII.

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<sup>47</sup> See discussion of NT in chapter three s3.3.3.

Market access is also affected in other modes of trade in services in the NII because only domestic insurance and reinsurance companies are permitted to underwrite domestic insurance and reinsurance except in ‘exceptional circumstances’ where the written permission of the Commission is obtained<sup>48</sup>. This means that cross border supply of reinsurance services in domestic insurance and reinsurance requires the reinsured to seek and obtain from the Commission a permission to do so after proving ‘exceptional circumstances’. The Act defines domestic insurance and reinsurance as including<sup>49</sup>:

- (a) fire insurance and reinsurance business;
- (b) motor insurance and reinsurance business;
- (c) liability insurance and reinsurance ;
- (d) life insurance and reinsurance;
- (e) accident insurance and reinsurance business; and
- (f) such other insurance and reinsurance business as the Commission may from time to time prescribe.

This implies that the a consumer has to mandatorily obtain written permission from NAICOM for cross border transactions in respect the above classes of insurance (a) to (f) but not for insurances and reinsurances of marine and aviation, oil and gas, engineering insurances including bonds and credit guarantees The condition for granting permission is ‘exceptional nature of the risk’ and the Act provides no

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<sup>48</sup> Insurance Act 2003 s72.

<sup>49</sup> *ibid* s72(2)(a-f).

definition for what qualifies as exceptional nature of risk. Therefore, it is left to the discretion of the Commission.

This suggests that the law recognises the four categories where cross border mode of trade is permitted are specialized insurance businesses often with huge sums insured and requiring skilled underwriters with large underwriting capacities. In actual fact, they are the bulk of insurance services sold mainly on cross border basis. It is presumed that the drafters of the Act had taken cognisance of the inadequacies of the NII and the fact that firms underwriting specialized risks in the NII depend heavily on foreign reinsurers for underwriting and rating. Therefore, cross border trade was allowed not only for reinsurance and also but also other classes of insurance. This was a good provision that supported liberalisation of the NII but which regrettably has been repealed by the NAICOM Annual Directives of 2008 and 2010.

The 2008 guidelines expanded the list of domestic insurances<sup>50</sup> for which the Commission's approval has to be obtained before cross border trade to include:

- ❖ Marine Hull insurance and reinsurance business; and
- ❖ Aviation insurance and reinsurance business;
- ❖ Any other business that the Commission may so prescribe from time to time.

Subsequently, the 2010 guidelines added oil and gas insurance and reinsurance to the list which now practically comprise almost all classes of insurance as provided under

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<sup>50</sup>IA 2003 s72 (2); see also discussion in s5.2above.

section 2 of the IA of 2003 with the exception of Bonds and Guarantee Insurances. This move aligned the Nigerian insurance legal framework with the Local Content Policy of the Federal government<sup>51</sup>. The effect of the above is that there is no cross border market access in the insurance industry in Nigeria except for bonds and guarantee insurance and reinsurance. This is a trade restrictive provision that definitely does not support liberalisation.

This restriction can only be abated with a written permit from NAICOM issued if and when the consumer satisfies the NAICOM that no domestic supplier is able to provide the cover required. The Commission is mandated to issue a ‘specific’ permit in writing. Specific is interpreted to mean that it must be specific to the risk for which permit is sought. This tedious ‘per risk approval’ process implies that a fresh permit would be required each time there is need for risk even of similar nature. This is a cumbersome and non-proportional provision that is restrictive to trade. The guidelines on oil and gas business<sup>52</sup> effectively affirmed the restrictions on cross border supply of insurance and reinsurance of oil and gas insurance business.

Similarly, foreign loss adjusters are barred from attending to claims in Nigeria except with the permission NAICOM and in collaboration with at least one local adjuster<sup>53</sup>. This provision is also restrictive to trade in services because it makes the participation of foreigner insurance agents in the NII difficult. An insurer requiring the services of

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<sup>51</sup> *ibid* s29.3. The Act had mandated that all insurances to do with Oil and Gas business be placed with domestic insurance companies to their ‘maximum capacities’ before the remaining risk is placed internationally through ‘an established international arrangement’ subject to the approval of the Commission.

<sup>52</sup> NAICOM, ‘Guidelines for Oil and Gas Business’ <http://www.naicom.gov.ng/index.php?p=Guidelines%20for%20Oil%20and%20Gas%20Insurance%20Business> accessed 12<sup>th</sup> August 2011.

<sup>53</sup> IA 2003 s48; NAICOM’s Guidelines for Oil and Gas Insurance Business (n52).

a foreign adjuster needs to go through the process of getting a written approval from NAICOM. Considering the limited administrative capacities of government agencies, this may cause unnecessary delay which makes the transaction unattractive to insurers. In essence, the provision is procedurally unreasonable<sup>54</sup>, restricts access for foreign loss adjusters and does not support liberalisation of insurance services. Due to the urgency often attached to claim administration in insurance easy access to foreign suppliers of insurance service should be enshrined in the legislations on insurance. Besides, Nigeria is a labour intensive country that could benefit from commitments in the temporary entry of professionals mode of trade in services. It is pertinent to note that Nigeria has no market access or NT commitment in the temporary entry of natural persons mode in the GATS. The law is therefore not violating any obligations. Nevertheless, liberalising this mode will make for greater openness of the NII and access to foreign markets.

There is also a 5% compulsory cession from insurance companies in the NII to African Reinsurance Company<sup>55</sup> known as Africa Re. This is the regional reinsurance company for Africa set up to reinsure insurance and reinsurance companies within Africa for the purpose of promoting growth and underwriting capacities in Africa to support African economic development. This compulsory cession is a provision under the Agreement Establishing African Reinsurance Corporation. Article 27 (2) of the Agreement provides that:

*“Each member shall undertake to guarantee, upon entry into force*

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<sup>54</sup> See discussion on dimensions of reasonableness in chapter four s

<sup>55</sup> Africa Re was set up under the Agreement to Establish African Reinsurance Corporation in 1976 by then 36 members of OAU now AU.

*of this Agreement, that all insurance and reinsurance establishments  
operating in its territory shall offer to place with the corporation  
a minimum of five percent of each of their reinsurance treaties  
both present and future including life treaties at term accorded to  
most favoured reinsurers”*

This is an agreement to which Nigeria is a signatory under African Union (AU). Though, it is ‘established both in international law and WTO that international law trade obligations prevail over national or regional rules’<sup>56</sup>, discrimination in regional integration is allowed under Article V of the GATS<sup>57</sup> as an exception to MFN obligations. The AU is the regional integration of African countries for GATS further allows for flexibility in the fulfilment of certain conditions<sup>58</sup> like the elimination of existing forms of discriminations and prohibition of new forms<sup>59</sup> which apply to this exemption<sup>60</sup>. Therefore, African countries can discriminate in form of compulsory cession to Africa Re by all insurance countries in Africa including Nigeria without violating MFN obligations. Consequently, the 5% compulsory cession to Africa Re is not a restriction within WTO and GATS. Nonetheless, in the GATS model of reforms, compulsory cession is eliminated in order to ensure a competitive and liberalised market. Though it is desirable that this practice be eliminated this is a regional effort and it would have adverse effect on the African region therefore, this thesis would suggest that compulsory session should be allowed since multilateral integration is

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<sup>56</sup> Thomas Cottier and Krista Schefer, ‘The Relationship Between World Trade Organisation Law, National and Regional Law’ (1998) 1JIEL 83, 85-6.

<sup>57</sup> See discussion on economic integration in chapter 3 s3(a)(vi).

<sup>58</sup> *ibid* subsection (2).

<sup>59</sup> *ibid* subsection (1).

<sup>60</sup> See discussion on non-discrimination in GATS in chapter 3 s3.2.2 (a)

being juxtaposed with regional integration effort. As noted in chapter one, this would afford other African countries the opportunity to leverage the gains of trade from Nigerian and would assist in making the country a regional economic giant which ought to be. This discrimination should be inscribed in Nigeria's Schedule of Commitments.

The law also mandates the insurance of all goods imported into Nigeria with domestic insurance service providers<sup>61</sup>. This is a trade restrictive position that may have consequences for the principle of reasonableness. This law is unfair to foreign producers and not entirely in line with international practices in the maritime business which is to insure at the point of departure and not with insurers at the destination of goods<sup>62</sup>. This provision is burdensome because it coerces foreign importers into placing insurance with firms they are not familiar with. The implication is that companies with existing annual marine insurance contracts in their home countries are forced to do double insurance which negates the principles of insurance<sup>63</sup>. This provision not only negates principles of reasonableness and international standards it also lacks proportionality. Disappointingly, it is stated in Nigeria's schedule of commitments as one of its General restrictions. Consequently, the law does not violate Nigeria's obligations under the GATS though in the pursuit of greater liberalisation, removal of such restrictions would positively affect Nigeria's liberalisation efforts.

The GATS model of reform also involves the adoption of risk based regimes as a tool

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<sup>61</sup> This law had been in operation for decades, since under the Insurance Decree of 1976 and it was codified into the IA 2003

<sup>62</sup> This has been the practice even in the early days of insurance at Lloyds coffee shop.

<sup>63</sup> This includes the principle of indemnity.

for liberation. Risk based regulation as noted earlier chapter two<sup>64</sup> are prudential provisions demanding that capital requirements are directly linked to the risks of firms. This means that the requirements of premium reserves, solvency and minimum share capital ought not to apply equally to all firms. Each firm must have specific requirements linked directly to its risk portfolio which is a function of its market share.

Prudential provisions in the IA are performance based regimes<sup>65</sup> which implies that they are not sensitive to the size and complexity of the risks written by insurance companies. The Act needs to be reformed to apply risk based regimes in line with current international prudential standards. The solvency regime is inadequate and weak. Considering the fact that 50% of insurance policies culminate in bad debts<sup>66</sup>, effective solvency regulations are needed ensure that insurers meet long term obligations. Performance based solvency margins are inadequate to address the predominant issues of bad debts and high lapse rate in the NII. For example, solvency provisions in the Act require all insurers to maintain a solvency margin of 15% of gross premium less insurance. This means the minimum solvency margin is ‘total admissible assets less total liabilities’ which ‘shall not be less than either 15% of net premium on the minimum paid up share capital whichever is higher’<sup>67</sup>. This rate has no reference to the differences in risk portfolios of insurance firms.

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<sup>64</sup> See s2.3.3.

<sup>65</sup> These are solvency regimes that are based on net premiums of insurance and reinsurance companies which is just gross premium minus reinsurance payments.

<sup>66</sup> Yemi Soladoye, ‘Insurance Sector Presentation’ (International Conference on Financial System Strategy 2020, Abuja, 2007) on 29<sup>th</sup>, slide 46  
<<http://www.cenbank.org/fss/tue/bsp/insurance/fss%202020%20-%20insurance%20presentation.pdf>>  
accessed 31<sup>st</sup> May 2010.

<sup>67</sup> NAICOM 2010 Operational Guidelines (Insurance and Reinsurance Companies) s3.7.

Similarly, the provisions for minimum share capital is based on the nomenclature of the insurance firm (life assurance business N150million (£566,000), general insurance business N200million (£755,000), composite insurance business N350million (£1.32million), and reinsurance business N350million (£1.32million)<sup>68</sup>. This provision has since been amended by the Federal Directive on Insurance Companies Capitalisation of 2005<sup>69</sup>, but it still follows the same categorisation of the Act except for the fact that composite insurance firms have been abrogated<sup>70</sup>.

There is an urgent need for the application of risk based approach to the IA in the NII. While not suggesting the adoption of Solvency 11<sup>71</sup>, the law should be dynamic enough to ensure that risk based measures that are attuned to the realities of the global financial market are in place in line with developments in the global integration of financial markets. The lack of risk based regulations has negative implications for liberalisation. Risk based regulations support regulatory effectiveness and the effectiveness of liberalisation programmes by ensuring positive gains accrue from it. In view of the fact that the IA capital and solvency provisions are inadequate to support effective liberalisation stresses the need for prudential regulatory reforms.

## **5.5 LAWS SUPPORTING LIBERALISATION OF NII**

The legal framework of the NII has measures which support liberalisation despite the analyses in the earlier two sections. This is notable in commercial presence mode with regards incorporation and registration; notification and remedial procedures in

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<sup>68</sup> Insurance Act 2003 s9(1)(a).

<sup>69</sup> The new capital requirements are life assurance business N2billion, general insurance and reinsurance business N10billion.

<sup>70</sup> This means a firm cannot write both life and general businesses.

<sup>71</sup> This is the risk based solvency regime being proposed by the EU.

licensing; provision of assistance by the NIPC; guarantees against expropriation of imported capital; non-existence of monopolies; non-discrimination for incorporated foreign firms in compulsory insurances; and insurances of government assets. Also in the cross border mode of trade, there is no collateralisation of assets for foreign reinsurance providers. Furthermore, there exist some principles based codes and directives that support liberalisation and are in compatible with the model of reforms being proposed.

The NIPC which is the foreign investment agency provides assistance for fast tracking incorporation and registration processes required by law such as under the Immigration Act and Investment and Securities Act etc. and coordinates investment through its ‘One Stop Services (OSS)<sup>72</sup>. NIPC is significant to the liberalisation of the NII in the commercial presence mode because it promotes transparency and provides ‘enquiry points’ in Nigeria. The NIPC also makes the process simple and fast through the OSS assistance in the interpretation and fulfilment of the laws. The NIPC Act also provides two significant guarantees which are the ability to transfer of capital, profit and dividends<sup>73</sup> and against expropriation<sup>74</sup>.

The expropriation provision guarantees that there shall be no nationalisation of assets and where such need arises in the national interest, a ‘payment of fair and adequate compensation’ would be made with undue delay and the investors’ interest can be determined in the court. These guarantees are significant especially against the

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<sup>72</sup> The OSIC simplifies the investment procedure in Nigeria and reduces processing time for compliance with legal requirements. It provides services such as incorporation, registration, residence and work permit and tax registration processing.

<sup>73</sup> Nigerian Investment Promotion Commission Act 2004 s24.

<sup>74</sup> *ibid* s25.

background of the indigenisation policy discussed in chapter one<sup>75</sup>. This provides some assurances for foreign investors and it is good for liberalisation.

Similarly, the Foreign Exchange Act allows foreign firms to import funds for the purpose of establishing commercial presence<sup>76</sup>. This can be done using cheques or other negotiable instruments and converted into naira<sup>77</sup> through an authorised dealer who is mandated to issue a Certificate of Capital Importation<sup>78</sup>. The relevance and legal importance of the CCI is that it confers on the holder the right to remit and repatriate the fund. It also guarantees the unconditional transferability of dividends, profits, payment to service loan where the foreign supplier had obtained a loan and remittance of proceeds and other funds in the event of sale or liquidation<sup>79</sup>. This is significant because it provides a means by which foreign suppliers can fund their branches in Nigeria and also facilitates remittance of profits and interest and the entire invested fund back net of taxes in the event of the exit of the foreign supplier. These provisions promote confidence in the NII because of the legal guarantees it offer foreign suppliers of service and therefore significantly contribute to the liberalisation of the sector in the commercial presence mode.

One of the main obligations in the GATS on licensing is prompt processing and the notification of an applicant ‘within a reasonable period of time’<sup>80</sup>. While no definition of reasonable time is given it is noted that obligations of this nature have attached

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<sup>75</sup> See s1.3.

<sup>76</sup> Foreign Exchange (Monitoring and Miscellaneous Provisions) (Forex) Act 2004 s15.

<sup>77</sup> *ibid* subsection (2).

<sup>78</sup> *ibid* subsection (1).

<sup>79</sup> *ibid* subsection (4).

<sup>80</sup> GATS Art VI(3).

some flexibility especially as it relates to developing countries like Nigeria<sup>81</sup>. This is considering the relative limited capacities inherent in the system. The IA provision is in tangent with the requirements of this obligation. The Act mandates the Commission to notify an applicant within 60days of submission of application if it decides not to license the firm<sup>82</sup>. This implies that there is a legal provision compelling the regulatory agency to notify within 60days if the application may be rejected. It could also be implied that applications that has been submitted in excess of 60days are going to be approved. Nigeria being a developing nation and bearing in mind its administrative capacities, 60days handling time for an application to establish commercial presence is reasonable procedurally. The time frame is proportional considering the need to verify documents and ascertain the suitability of the applicants.

Furthermore, there are remedial procedures for administrative decisions of NAICOM in line with the requirement of the GATS. An applicant who receives a notice of intention to reject its application from the commission is allowed an appeal to the minister within 30days of receipt of the letter from the Commission<sup>83</sup>. The minister is mandated within 60days to decide and convey its decision on the appeal to the applicant through the Commission. This provision is fair, clear, very objective, reasonable and impartial and in line with GATS requirement for prompt review of administrative decisions<sup>84</sup> and also supports the liberalisation of the NII.

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<sup>81</sup> Keiya Iida and Julia Nielson, 'Transparency in Domestic Regulations: Practices and Possibilities' in Aaditya Mattoo and Pierre Sauve (eds) *Domestic Regulation and Service Trade Liberalization*, (World Bank and OUP 2003) 17.

<sup>82</sup> IA 2003 s7(1).

<sup>83</sup> *ibid* section 7(2).

<sup>84</sup> GATS Article VI:2(a).

Other measures supporting liberalisation in the commercial mode is the abolition of provisions requiring localization of assets or collateralization for foreign reinsurers or right of first refusal for any domestic reinsurance supplier in Nigeria<sup>85</sup>. It is also refreshing to note that there are no legal restrictions on equity shareholding or discrimination with regards to participation of foreign firms in compulsory insurances or the insurances of government assets. All legislations and measures apply to both domestic and registered foreign providers equally. Foreign insurance providers licensed in Nigeria are permitted to write all classes of insurance including compulsory insurances. The same applies to insurances of state owned enterprises.

There are no statutory provisions for any form of monopoly or exclusive provider. In actual fact, the practice of having government owned insurance companies exclusively providing insurance on government assets or enterprises had been eradicated as a result of the privatisation exercise discussed<sup>86</sup>. Consequently, local branches of foreign insurance companies are free to compete with other domestic suppliers for any business of government without restrictions. However, it is pertinent to note that the Nigerian agricultural Insurance Corporation (NAIC) a government owned insurance company set up to implement the federal government's Agricultural Scheme is sometimes viewed as a monopoly. NAIC is the means by which government provides insurance cover at a subsidized premium rate for the development of the agricultural sector. This measure is also allowed for developing countries in the GATS<sup>87</sup>. Other insurance companies are not prohibited from writing agricultural insurance in Nigeria. NAIC is set up for just a few categories of

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<sup>85</sup> This used to be the case under the Nigerian Reinsurance Decree of 1977 where 20% compulsory cession and right of first refusal was granted to Nigerian Reinsurance Corporation.

<sup>86</sup> See discussion chapter one s1.5.

<sup>87</sup> *ibid* Article XV (1), a provision allowing subsidies for development programs of LDCs.

agricultural risks<sup>88</sup> and it competes with other private insurers for other classes of commercial insurances. Nevertheless, the GATS does not prohibit monopolies but requires that such monopolies should not act in a manner inconsistent with MFN obligations of members in committed sectors and should not abuse its monopoly position<sup>89</sup>.

Pension management was separated from insurance services due to the reforms that led to the enactment of the Pension Act of 2004. This was as a result of government's inability to pay pensioners in the old system. Insurance companies no longer provide pension services unless they register as either a Pension Fund Administrator (PFA) or Pension Fund Custodian (PFC) with the Nigerian Pension Commission (NPC). Nonetheless, a cursory analysis of pension administration is necessary under the parameters for insurance liberalisation since pension is viewed as part of insurance.

The NPC established under the Pensions Act of 2004 (PA)<sup>90</sup> has powers to supervise, make regulations or guidelines on pension matters in Nigeria<sup>91</sup>. The NPC is authorised to grant licenses to firms applying as PFA or PFC who are required to be registered as limited liability companies with minimum share capital of N150million and N5billion respectively with the latter having a balance sheet reading of at least N125billion<sup>92</sup>. There are no provision prohibiting foreign pension providers except

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<sup>88</sup> Nigerian Agricultural Insurance Corporation Decree of 1993, s8 (1) (a and b); risks covered are fire, lightning, windstorm, flood, drought, pests or invasion of animals for crops and for livestock, Fire, lightning, storm, flood, disease or accident.

<sup>89</sup> *ibid* Article VIII (1)&(2)

<sup>90</sup> PA 2004 s14.

<sup>91</sup> *ibid* s20,29 and 97.

<sup>92</sup> *ibid* s49 and 52.

that requiring local incorporation. Therefore, there is no restriction to liberalisation of insurance with regards to pensions business.

Principles based regulations also exist in the legal framework of the NII. The NAICOM Code of Good Corporate Governance for Insurance Industry in Nigeria and Know Your Customer (KYC) Guidelines is significant as tools of liberalisation of the NII.

The code of corporate governance was the first attempt by NAICOM at PBR and it stressed the principle of good governance, accounting disclosure and transparency. The code made provisions for a proactive, responsive and committed board. It also entails compliance to rules and regulation, exercise of shareholders' right and unambiguous disclosure of insurance firm's financial condition while stressing transparency in organisational operations<sup>93</sup>. This regulation complements the IA 2003 provision for code of conduct<sup>94</sup> and it emphasised the need for good corporate governance for competitiveness and integrity. It made provisions for the constitution of boards of insurance companies, board committee and meetings. It also required the application of accounting principles with international accounting standard to mention a few. This code for the first time made the board of insurance companies the focal point in corporate governance in line with the requirement of IAIS core principles on corporate governance<sup>95</sup>. It effectively promotes principles which favour the liberalisation for the NII.

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<sup>93</sup> 'Code of Good Corporate Governance for Insurance Industry in Nigeria' 2009 s4.

<sup>94</sup> IA 2003 s79.

<sup>95</sup> See discussion of corporate governance in chapter four s4.4.3.

NAICOM's Know Your Customer (KYC) Guidelines<sup>96</sup> is another principle based measure. It derives partly from the ICPs on Fraud and Anti-Money Laundering<sup>97</sup> and also in response to the customer identification programme which was introduced into Nigeria by the Money Laundering Act of 2004. The regulation mandates all financial institutions to verify customer identity and address before establishing any fiduciary transaction or business relationship<sup>98</sup>. The KYC code has positive implications for liberalisation because it promotes transparency and the integrity of the NII.

Furthermore, steps have been taken towards the adoption principles of international standards in financial reporting in NAICOM's 2011 guidelines<sup>99</sup>. The Commission notified insurers and reinsurers about the Federal Government of Nigeria's adoption of the roadmap to the International Financial Reporting Standards (IFRS) and it requested from insurers and reinsurers alike an IFRS conversion plan and gave a time frame within which such plan must be communicated to the Commission.

Other liberal provisions in the NII legal framework include the transparency provisions in the relating to rejection of an application to register either as a general business insurer or as a life insurer. The law requires that where the application for registration is rejected<sup>100</sup> it must be published in the federal gazette. In cases of cancellation of registration for failing to meet up with various requirements of the IA, the Commission is mandated to publish the rejection in any medium with wide

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<sup>96</sup> NAICOM, 'Know Your Customer Guideline' <<http://www.naicom.gov.ng/Index.php?p=Customer%20Guideline>> accessed 12<sup>th</sup> August 2011.

<sup>97</sup> See discussion in chapter 44.4.3 on IAIS ICPs 27& 28.

<sup>98</sup> Money Laundering (Prohibition) Act 2004, s3.

<sup>99</sup> NAICOM, 'Operational Guidelines 2011, one for Insurers and Reinsurers' section 6, <<http://www.naicom.gov.ng/index.php?p=policy&subpage=SOLVENCY%20MARGIN>> accessed 16<sup>th</sup> August 2011.

<sup>100</sup> IA 2003 s7 (7).

publicity. Furthermore, in cases of amalgamation, transfer or acquisition of an insurance company, it is mandated that a notice of intention to amalgamate, transfer or acquire should be published 3months prior to the submission of an application for that purpose with the commission<sup>101</sup> in at least 5 national newspapers. Finally, the Commission is obliged to publish the names of insurers who withdraw from the mandatory statutory deposit with the CBN and don't repay back within 30days in the newspaper<sup>102</sup>. These provisions vary in terms of the form of publication required. The Act has mandated publication in newspapers for situations of serious implication to the industry, such as amalgamation, transfers and acquisition where the publications is required to be in 5 national newspapers. These disclosure provisions have reflected the principle of proportionality which is significant in liberalisation of the NII.

There are also transparency provisions for financial statements and reports. Insurance firms are financial reports are required to be publicly available by law so that they could be accessed by interested parties possibly looking to invest in such companies. Insurers are mandated to publish their 'general annual balance sheet together with profit and loss accounts in at least one newspaper having wide circulation in Nigeria'<sup>103</sup>. This must first be approved by the commission. This provision is important because it supports liberalisation in line with the WTO/GATS model of reform by contributing to the general transparency of the NII and providing the important oversight function of the commission to ensure that the statements are in order before being published in the newspaper.

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<sup>101</sup> IA 2003 s30 (4).

<sup>102</sup> *ibid* s10(5).

<sup>103</sup> IA 2003 s26 (4) and s27(6).

There is also public availability of the IA and other related legislation on electronic media, government offices etc. at Nigerian embassies all over the world.

The exit provisions for insurance companies reveal good regulatory principles which support liberalisation. A petition for winding up<sup>104</sup> may emanate from the policyholders with the approval of the commission or from the commission itself<sup>105</sup>. This is a legal instrument empowering policyholders to protect their interest. Insurers involved in life insurance businesses are however not allowed voluntary winding up except for the purpose of amalgamation, transfer or acquisition<sup>106</sup>. This is logical and necessary to protect policyholders with interests in accumulated life funds which may be lost in such circumstances. These provisions also promote the principles of reasonableness and the rule of law ensuring that all stakeholders have a fair chance of protecting their interests before the court. Policyholders are also adequately provided for in the event that an insurance company ceases business. These provision support principles of international trade law and are suitable for liberalisation.

## 5.6 CONCLUSION

This chapter has benchmarked the legal framework of the NII against the GATS model of legislative reforms for liberalisation. It highlighted measures that are compliant, non-compliant and those that support liberalisation of the NII generally

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<sup>104</sup> The winding up petition is generally governed by the company law in Nigeria but the IA makes provisions giving right to policyholders.

<sup>105</sup> A petition to wind up an insurance company may be presented to the court by 50 policyholders with insurance policies with the company for at least 3yrs with the approval of NAICOM. Policyholders' rights though derived under the IA can only be enforced in compliance with winding up provisions of s408 and 409 of the Companies and Allied Matters Act of 2004 Companies where the company is unable to pay its debt or it is equitable that the company be wound up among other reasons.

<sup>106</sup> *ibid* s33; However, non-life companies can wind up voluntary under the company law regime.

Measures that are non-compliant and need to be changed are mainly the silent embargo on licensing of new insurance firms, the restrictions on cross border reinsurance and non-application of international standards to financial reporting.

The NII legal framework is more favourable to commercial presence though more liberalisation would still be required in that mode. Some compliant measures were not sufficiently liberal such as those dealing with registration and licensing. There is need to streamline the process of licensing and registration of foreign suppliers in the commercial presence mode. In some developing countries where insurance sector liberalisation had taken place, the laws relating to foreign insurers participation has had to be streamlined to ensure that regulations do not become trade barriers<sup>107</sup>.

There is need to liberalise other modes too especially the temporary entry of persons and consumption abroad mode. Actually, there is no law relating to the latter within the legal framework of the NII. These transactions go unnoticed because they occur outside the jurisdictions of the law and the law does not recognise them<sup>108</sup>. In the temporary movement of natural persons mode, removal of the restrictions on the entry of adjusters would enhance the liberalisation process of the NII.

Reforms should be geared towards enhancing liberalisation in the cross border mode especially in classes of insurance and reinsurance business where Nigeria currently lacks the skills and capacities. These are engineering, oil and gas and some transportation insurances such marine and aviation. There is also need for the

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<sup>107</sup> For example, China enacted The Regulations on Administration of Foreign Funded Insurance Companies' in 2002 which gave a grace period of two years of practice to submit an application for licensing. It also relaxed the process of licensing by making it very easy for foreign insurance companies to comply. In less than 10years after reforms, number of insurance companies grew from about 10 to 61 of and foreign insurance companies rose from nothing to 21.

<sup>108</sup> Nigeria remains unbound in its schedule of commitments in the GATS under this mode.

application of national treatment principles to ensure the law is more favourable than it is for foreign participation. Though the NII laws apply equally to foreign and domestic firms, it is more favourable to the domestic than foreign suppliers therefore it does not promote competition.

The framework has no risk based provisions for all its prudential regulations consequently there is a need to adopt risk based standards to fortify the market against insolvencies before effecting further liberalisation<sup>109</sup>. The need for risk based regimes is once again reemphasised in this thesis as necessary for effective liberalisation. It is commendable that some principle based measures were available such as the Code of Corporate Governance and KYC code. The main instrument of regulating insurance the IA 2003 had a few principles inherently applied but unfortunately most of the provisions lacked the principle of reasonableness proportionality and transparency.

Areas for which reforms are further suggested for effective liberalisation include the adopting of risk based regulations and principle based regimes in the regulatory framework. Laws need to be in place that supports investor confidence through greater transparency. Restrictions which require the obtaining of written permission for reinsurance and loss adjusters should be replaced with PBR which focuses on goals and systems other than prescriptive regimes<sup>110</sup>. These restrictive elements have serious implications for the liberalisation of the NII. The delay in adopting international standards in transparency and solvency regulations portrays lack of prudence in the legal framework of the NII.

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<sup>109</sup> See chapter 2 for discussion on the need for risk based regulations in insurance.

<sup>110</sup> See discussion regulatory regimes in chapter two s2.3.2.

In summary, the legal framework of Nigeria is a highly prescriptive regime<sup>111</sup> and most of the legislations in the NII regulatory framework are outdated, obsolete<sup>112</sup> and inadequate. The regulatory approaches<sup>113</sup> of the laws are mainly restrictive and tend to protect the domestic providers of insurance.

The analysis revealed NAICOM's continuous strive at benchmarking its rules, laws and regulatory approaches against international best practices<sup>114</sup> with Nigeria's membership of international standard setting organisations such as IAIS AND International Financial Reporting Standards (IFRS) is commendable. The implication is a gradual adoption of international standards which portrays positive strides for liberalisation of the NII.

The next chapter reviews the supervisory framework of the NII liberalisation against the institutional aspects of the GATS model of reforms for liberalisation. This analysis would complement the analysis in this chapter and would allow for a more comprehensive view of the extent of liberalisation of the NII.

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<sup>111</sup> See chapter 2 (n181).

<sup>112</sup> CAMA since 1990 and the Immigration Act since 1963.

<sup>113</sup> See chapter 2 s4(b)(ii).

<sup>114</sup> NAICOM, 'NAICOM Corporate Strategic Plan 2011-2013, <  
<<http://www.naicom.gov.ng/index.php?p=NAICOM%20Corporate%20Strategic%20Plan%202011-2013>> accessed 15<sup>th</sup> August 2011.

## **CHAPTER SIX**

### **THE NII AND THE INSTITUTIONAL PARAMETERS OF LIBERALISATION**

#### **6. INTRODUCTION**

The last chapter critically reviewed the legislative framework for the NII liberalisation against the legislative model of reforms for insurance liberalisation identified in chapter four. The analysis revealed measures that were non-compliant with the model and also those that were compliant but not sufficiently liberal. Also identified were some measures that were already supportive of liberalisation. The chapter concluded with a summary of areas in the framework requiring reforms. This chapter continues the legal analysis by examining the NAICOM Act of 1997 which established NAICOM vis-à-vis the institutional and supervisory model for liberalisation of insurance highlighted in chapter four.

The chapter is divided into six sections with the first restating the institutional model of reforms for insurance liberalisation while the second gives a brief review of the NAICOM Act of 1997. The third section examines the provisions of the Act for supervisory objectives *viz – a viz* the model for legal reforms. The fourth and fifth sections contain the analyses on supervisory authority and supervisory process respectively. The conclusion of the chapter is contained in the sixth section highlighting the institutional challenges of the NII liberalisation from the analysis of the Act

## 6.1 THE INSTITUTIONAL MODEL OF REFORM FOR LIBERALISATION

This model focuses mainly on issues relating to supervisory objectives, supervisory authority (with powers, legal protection, financial resources, independent and accountable, sufficient well trained staff); supervisory process that is transparent including the surveillance structures; and supervisory cooperation.

This model has an independent supervisory authority with clearly defined objectives which focuses on the promotion of an efficient, clear and safe market for policyholders<sup>1</sup>. The agency also possesses adequate powers, and resources. Powers include adequate supervisory powers to perform technical functions such as surveillance and monitoring and also for every day running of the agency. On the other hand, resources of this agency include sufficient funds, well trained personnel with legal protection. Specifically, there is sufficient budget to attract, train and maintain necessary personnel<sup>2</sup> and adequate staff with “knowledge in insurance, actuarial science, law and wide experience”. The agency staff and representatives have legal protection while performing the functions of authority.

Furthermore, the agency is independent but accountable to government and the public<sup>3</sup>. The supervisory agency has proper governance structure including internal audit and it is managed prudently. There are clear procedures for appointment and removal of members of the governing board and public disclosure of removal and rational for it is mandatory. There is also a clearly defined relationship mechanism

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<sup>1</sup> IAIS, ‘Insurance Core Principles and Methodology’(2003) 9  
<[http://www.iaisweb.org/\\_temp/Insurance\\_core\\_principles\\_and\\_methodology.pdf](http://www.iaisweb.org/_temp/Insurance_core_principles_and_methodology.pdf)> accessed 9th October 2009.

<sup>2</sup> IAIS ICP 3.

<sup>3</sup> IAIS(n1) 10-11.

between the agency and the government that ensures freedom of the supervisory agency from any form of influence. This entails a clearly defined funding structure which does not undermine the independence and freedom of the agency to allocate its resources. In maintenance of accountability, representatives of the agency are obliged to publicly explain its objectives and report to the public its activities and performance in achieving the objectives. In a nutshell, the supervisory agency provide rational for its decisions<sup>4</sup> to the government, insurers being supervised and the public. The issue of transparency is vital therefore the regulatory authority conducts its functions with public knowledge and engages in consultations on the supervisory process. Proposed and existing regulations are made available for public scrutiny through established means for interaction between the supervisory agency and the public.

Furthermore, in this model the agency cooperates with other regulators in the financial sector by sharing information with relevant supervisory authorities; an action critical to the supervision of international insurance conglomerates and insurers that are active internationally. The agency also shares information with foreign supervisors especially where a domestic insurance intends to engage in cross border trade.

Finally, in the institutional model of reforms, there are surveillance structures in place in form of on-site, off-site and on-going supervision. This ensures no insurer or reinsurer escapes supervision, adequate monitoring and active analysis of risks of individual insurers, insurance groups, the market and the environment is done. The

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<sup>4</sup> ibid p12

supervision is risk based and frequency of on-site supervision is dependent on the risk profile of individual firms and results of off-site analysis of reports submitted. Publicly disclosed sanctions that are clear and objective are given to non-complying and erring firms. In-depth market qualitative and quantitative analysis to identify the risk and vulnerability with prompt intervention will reduce chance of future problems should be done. The agency therefore engages in both preventive and corrective measures to ensure an efficient and competitive market. The agency's analysis however involves not only domestic but also international trends which may impact the market<sup>5</sup>.

## **6.2 NIGERIAN INSURANCE COMMISSION (NAICOM) ACT 1997<sup>6</sup>**

This Act came into force on the 10<sup>th</sup> of January 2004 and it repealed the Insurance Decree of 1991. The 1991 Decree institutionalised insurance supervision for the first time in Nigeria by creating the Nigerian Insurance Supervisory Board (NISB). However, NAICOM Act established NAICOM and this replaced the NISB as the supervisory authority for the insurance sector.

The Act contains 66 sections divided into 8 parts which provide for the establishment of the Commission, its governing board<sup>7</sup>, its object and functions<sup>8</sup>, staffing<sup>9</sup> and financial aspects<sup>10</sup> including levy collections<sup>11</sup>. It also provided for the supervisory function of NAICOM<sup>12</sup> and procedures for dealing with failing or failed insurance

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<sup>5</sup> IAIS (n1) 23-29

<sup>6</sup> The law was enacted as a Decree but was codified in 2004.

<sup>7</sup> National Insurance Commission Act of 1997 s1-5.

<sup>8</sup> *ibid* s6-9.

<sup>9</sup> *ibid* s10-15.

<sup>10</sup> *ibid* s16-24.

<sup>11</sup> *ibid* s25-30.

<sup>12</sup> *ibid* s31-40.

firms<sup>13</sup>. There are also miscellaneous provisions<sup>14</sup> for jurisdiction and prosecution, other powers of the Commission etc.

### 6.3 Supervisory Objectives

The Act provides clearly defined objectives of the Commission. The principal objectives of the Commission are to ‘ensure the effective administration, supervision, regulation and control of the insurance business in Nigeria’<sup>15</sup>. This is very clear and unambiguous requiring effective control of the NII. However, there is no emphasis on the equitable and beneficial interest of policyholders which should actually be the focus of insurance regulations as noted in chapter two<sup>16</sup>. In the same vein, no reference is made to regulatory efficiency. Effectiveness does not represent efficiency because it only emphasises getting things done well. However, efficiency has reference to cost. It implies the achievement of a goal at the cheapest cost. This has implications for the principles of proportionality<sup>17</sup>. A regulation is not proportional if the cost outweighs the benefits. Proportionality is a liberalisation principle of the WTO/GATS framework and therefore, the objectives need to stress both regulatory and market efficiency as a goal. This also has repercussions for competition and liberalisation. If there is regulatory inefficiency, the insurance market is also bound to be inefficient and would be unable to compete globally. There will be limited prospects for liberalisation and it would be difficult to fulfil the goal of economic growth in Nigeria. Nonetheless, the clearly stated objectives support liberalisation

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<sup>13</sup> *ibid* s41-48.

<sup>14</sup> *ibid* s49-66.

<sup>15</sup> National Insurance Commission Act of 1997 s6.

<sup>16</sup> See discussion in chapter two s2.5

<sup>17</sup> *ibid*.

because regulatory effectiveness is also germane for successful liberalisation<sup>18</sup>.

Though the Act does not reflect the policyholder as the focus of NAICOM's objective, there are ample provisions in the NAICOM Act addressing the interests of the policyholders. With every regulatory power the Act provides a safeguard for the policyholder and emphasises the policyholders' interests. Section 7(h) of the Act provides that the protection of insurance policyholders, beneficiaries and third parties as one of the functions of the commission. It also provides that on the application by a policyholder the commissioner may order a special inspection of the books and activities of an insurance institution<sup>19</sup>. Furthermore, the commission may exercise its powers of intervention if it considers it desirable to protect policyholders against the risk of the insurance institution not being able to meet its liabilities<sup>20</sup>. The commission could also require an insurance institution to take some appropriate actions for the purpose of protecting potential or current policyholders<sup>21</sup>. The policyholder's interest is also provided for where an insurer is in an unsound condition likely to hazard policyholders<sup>22</sup>. Finally the commission is prohibited from taking over a failing or failed company if it would be detrimental to the interest of the policyholder<sup>23</sup>. It is appropriate to note also that the Act makes provisions for the establishment of complaints bureau<sup>24</sup> as part of the functions of the Commission. This strengthens the consumer protection provisions. However, it fails to provide for the composition, powers and functions of this bureau. This is left to the discretion of the Commission.

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<sup>18</sup> *ibid* s2.4.1.

<sup>19</sup> NAICOM Act of 1997 s35 (e) (ii).

<sup>20</sup> *ibid* s37 (a).

<sup>21</sup> *ibid* s40.

<sup>22</sup> *Ibid* s41 (1) (b) (ii).

<sup>23</sup> *ibid* s45 (2).

<sup>24</sup> *ibid* s8 (a).

The Act by these provisions reiterates the importance of policyholders' protection for effective supervision and regulation of insurance services. These are also consistent with objectives of the WTO/GATS framework of liberalisation which emphasises socio-economic well-being of citizens of its members. They also accentuate the reinforcement of the market by purging it of unsound and nonperforming insurers. A healthier market will facilitate successful liberalisation and enhance the growth potentials of insurance services.

Consumer protection has macro and micro elements both of which are equally important. On the macro-economic level, they are protected against insolvencies in the industry while on the micro-economic level, against bad market practices<sup>25</sup>. The NAICOM Act emphasises both dimensions of protection in the statutory functions of the NAICOM.

This thesis posits that the provisions for consumer protection need to be further strengthened especially in a liberalised NII<sup>26</sup>. Liberalisation brings about more competition and this may result in unsound market practices that make consumers vulnerable<sup>27</sup>. To forestall this situation, the NAICOM Act and other relevant regulations need to emphasise policyholders' protection for effective liberalisation. Reforms must amend the laws to include special provisions protecting the rights of consumers in pre-contract and post contract situations to reduce the incidence of unfair practices among insurers.

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<sup>25</sup> *ibid* see chapter two s2.4.1

<sup>26</sup> UNCTAD, 'Review of Critical Areas with Regard to Insurance Legislation, Regulation and Supervision, Establishment of effective insurance regulatory and supervisory systems' (1995) Study by the UNCTAD secretariat, TD/B/CN.4/52, para 4, [http://unctad.org/en/docs/sddins10\\_en.pdf](http://unctad.org/en/docs/sddins10_en.pdf) > accessed 22nd April 2011.

<sup>27</sup> NAICOM Act of 1997 para 11.

Other functions of the Commission include the establishment of standards; approval of premium and commission rates and policy terms;<sup>28</sup> regulating transactions between insurance firms<sup>29</sup>; advising government on insurance matters<sup>30</sup>; publishing and sale of annual statistics on insurance industry<sup>31</sup>, and policy holders' protection,<sup>32</sup> and the protection of the strategic assets of the Federal Republic of Nigeria<sup>33</sup>. These functions are all relevant for the liberalisation framework of the GATS. Proper regulations, establishing standards are essential for a liberalised NII, and publishing reports on the industry promotes transparency. Proper supervision of rates, premium and policy terms protect policyholders from bad market practices. However, these provisions do not have benchmarks for reference. There is no reference to any regulatory principle or international standards. This has also been left to administrative prerogative.

The Act also provides another function for the Commission of significance to liberalisation of the NII. The Commission is charged with liaising and advising government agencies on matters relating to technical agreements on insurance in which Nigeria is a signatory<sup>34</sup>. This suggests that the Commission has statutory powers to advise government on commitments and liberalisation within the GATS. Though this is a consultative role, it indicates that the Commission is in the position to influence the liberalisation of insurance either positively or negatively. It is imperative therefore that the Commission has adequate experienced staff to accomplish this significant responsibility.

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<sup>28</sup> *ibid* s7 (b)(c)(g).

<sup>29</sup> *ibid* s7 (e).

<sup>30</sup> *ibid* s7 (f).

<sup>31</sup> *ibid* s7 (i).

<sup>32</sup> *ibid* s7 (h).

<sup>33</sup> *ibid* s7 (d).

<sup>34</sup> *ibid* s7 (j).

The liberalisation framework of the WTO/GATS is rules and principles based requiring the law to be detailed enough to remove inconsistencies in its interpretation and application. The areas of reforms with regards to regulatory objective and function include need to stress the significance of supervision in the interests of policyholders, secondly to promote supervisory efficiency and finally to provide detailed provisions for precise interpretation to the law.

#### **6.4 Supervisory Authority**

The NAICOM Act established the Commission as a body corporate with perpetual succession and common seal<sup>35</sup> with an organisational structure which include a governing board<sup>36</sup> and executive management comprising the commissioner of insurance<sup>37</sup> and two deputies to handle technical operations and finance and administration respectively with relevant qualification provisions<sup>38</sup>. The composition of the board of NAICOM is significant to the liberalisation of the NII. This is because the governing board is empowered to manage and supervise the Commission, give policy direction and appoint necessary staff including directors<sup>39</sup>. This is important because the board determines the policy direction and ultimately the effectiveness of the Commission. It is therefore important that members of the board have relevant skills and qualification. It is equally important that a very good corporate governance regime is in place to enhance the prospect of regulatory effectiveness facilitated by good regulatory governance. Successful liberalisation processes accentuates the need

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<sup>35</sup> *ibid* s1(2).

<sup>36</sup> *ibid* s2.

<sup>37</sup> *ibid* s10.

<sup>38</sup> *ibid* s11.

<sup>39</sup> *ibid* s14 (1).

for regulatory effectiveness.

The NAICOM board consists of 11 members comprising a part-time chairman, commissioner of insurance and two deputy commissioners appointed by the Head of state<sup>40</sup> and representatives of the Federal Ministry of Finance, Central Bank of Nigeria, Chartered Insurance Institute of Nigeria (CIIN) and Federal Ministry of Commerce and Industry<sup>41</sup>. Three part-time members also represent the interest of the public on the board<sup>42</sup>.

This is a reasonably sized board with diverse membership which could translate into significant benefits for the Commission because of the wealth of experience pulled together. This would also enable effective management of the Commission. The board also includes representatives of the public which implies that the Act recognises that the whole essence of regulating insurance is to protect policyholders and the public at large. However, the method of appointment of the members leaves room for politicisation of the process since all members are appointed by the head of state except for the ex-officio members. This might have negative consequences for the degree of independence of the Commission. However, with experienced members, the board may positively influence the prospects of the liberalisation of the insurance industry.

## **Powers**

The NAICOM Act makes provision for both the administrative powers needed for

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<sup>40</sup> *ibid* s2 (2).

<sup>41</sup> *ibid* s2 (1)(b).

<sup>42</sup> *ibid* s2 (1).

every day running of the Commission and supervisory powers which enable it to perform its technical functions.

The administrative powers of the Commission are contained mainly in section 8 of the Act and these include the power to acquire offices<sup>43</sup>, establish zonal offices<sup>44</sup> and borrow money<sup>45</sup>. The Commission does not require the approval of the minister for the powers in this section. The other administrative powers are specifically related to the appointment of staff. The Act gives the governing board the power to employ<sup>46</sup>. The power to determine the remuneration and conditions of service of staff are however subject to the approval of the minister<sup>47</sup>. This has substantial repercussions for the budgetary independence of the Commission<sup>48</sup>.

The supervisory powers provided by Act for the NAICOM include powers of inspection<sup>49</sup>, of actuarial investigation<sup>50</sup> of intervention in troubled insurance firms<sup>51</sup> and issuance of guidelines for the industry<sup>52</sup>. The Commission's power also includes protection of policyholders<sup>53</sup> and managing failing or failing insurance firms<sup>54</sup> through prosecution of individuals or organisations connected<sup>55</sup>, removal of directors<sup>56</sup>, revoking of license<sup>57</sup> or appointment or assuming control of the

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<sup>43</sup> *ibid* s8(d).

<sup>44</sup> *ibid* s8(e).

<sup>45</sup> *ibid* s8(c).

<sup>46</sup> *ibid* s14.

<sup>47</sup> *ibid* s15.

<sup>48</sup> This is discussed in detail under independence and accountability.

<sup>49</sup> NAICOM Act of 1997 s50& 32

<sup>50</sup> *ibid* s36.

<sup>51</sup> *ibid* s36-9.

<sup>52</sup> *ibid* s49

<sup>53</sup> *ibid* s40

<sup>54</sup> *ibid* s41.

<sup>55</sup> *ibid* s48.

<sup>56</sup> *ibid* s41 (2) (d).

<sup>57</sup> *ibid* s44.

organisation among other actions<sup>58</sup>.

These are tremendous powers which allows for effective surveillance, supervision and regulation of the industry. These are consistent with the powers necessary for promoting a healthy the sector going by IAIS principles. The Act identifies the NAICOM as the supervisory authority and gives the Commission power to issue and enforce rules by administrative means. The supervisory powers grant the Commission effective tools to facilitate a healthy and sound NII. The only shortcoming of these provisions is that the approval of the minister is needed to enforce some of the powers.

For example, the Commission cannot assume control of a failing or failed insurer<sup>59</sup> nor can it prosecute persons connected<sup>60</sup> without the approval of the minister. For revocation of licenses of failed insurers<sup>61</sup>, the approval of the head of state is required in addition to that of the minister. The implication is that the Commission has powers but no corresponding authority. It is not insulated from the politics of government and this portrays the lack of supervisory independence which is discussed in detail later<sup>62</sup>.

In summary, the Act has made powers available for the administrative and technical operations of the Commission. However, these powers in some instances are not independent of the executive arm of government. There is a real possibility of political influence on the activities of the Commission. This may affect the credibility of the Commission and impact negatively on regulatory effectiveness and successful

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<sup>58</sup> These supervisory powers are discussed in detail under supervision s6.5.

<sup>59</sup> NAICOM Act of 1997 s42 (1).

<sup>60</sup> *ibid* s48.

<sup>61</sup> *ibid* s44.

<sup>62</sup> See discussion on independence.

liberalisation.

### **Adequacy of Resources**

The provisions for financial resources of the Commission under the NAICOM Act include money assigned by the federal government, one percent levy on gross income of insurance institutions, income from investments of the Commission, borrowing from approved sources, income from fees and penalties and finally gifts or endowments<sup>63</sup>. The implication is that the Commission has fee-based funding which is a good practice also facilitating budgetary independence of the regulator. However, the Act also made specific provisions on how these funds should be expended. The Act directs that 50% should be spent on operations (i.e. administration including board expenses, salaries, remuneration and pension gratuities of staff), 30% on educational assistance, and 20% for the development of the NII. Further, it is pertinent to note that the Commission is in control of its budget since it only needs to be presented to the governing board of the Commission. The ‘money assigned to the Commission by government’ is difficult to interpret simply because it is not explained anywhere in the Act. Furthermore, since there is no public availability of the audited account of the Commission, it would be difficult to determine the adequacy or sufficiency of the funds available to the Commission. The Act is silent about how capital expenditures would be met. The only provision related to capital is in s18 (d) where the Commission is required to use part of the operating fund for the maintenance of any property vested in the Commission. This by implication means

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<sup>63</sup> NAICOM Act of 1997 s16 (1) (2).

that some properties may be vested in the Commission and property is a form of capital.

There are a lot of ambiguities in the provisions on financial resources that makes it difficult to understand. Three possible interpretations are relevant to capital expenditure. The first is that the Commission would fund its capital expenditure; an option that is most unviable knowing it is only allowed 50% of its income. The second alternative is that this would be provided by the supervising ministry which portrays lack of independence. The third option is that ‘money assigned by government’ may actually refer to monies assigned for capital expenditure which has the same implication as the second alternative. One fact which is evident judging by the provisions of the Act is that there are inadequate provisions for financial resources in the NAICOM Act of 1997.

This provision appears restrictive on income and expenditure and portrays inadequate funding. The consequences of inadequate financial resources are that the Commission cannot function effectively because it has further implications for staffing which is discussed below.

Aside the provisions of the members of the board, the Act also makes provisions for a chief inspector<sup>64</sup> and gives the option of either appointing an actuary or securing the services of an actuarial consultant<sup>65</sup>. It further empowers the board to employ as many staff as it is expedient and necessary for proper and efficient performance of the functions of the Commission<sup>66</sup>. This implies that the board had the authority to employ as much as it deems necessary for the operations of the Commission but

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<sup>64</sup> *ibid* s31(2)(a).

<sup>65</sup> *ibid* s36.

<sup>66</sup> *ibid* s14.

giving consideration to cost<sup>67</sup>. There appears to be no restrictions on the number of staff employable given the simple interpretation of the provision. However, when juxtaposed with provisions on financial resources, it becomes apparent that the available financial resource will ultimately determine the size of staff. This is coupled with the fact that the board needs to obtain the approval of the minister for the remunerations and conditions of service of staff. Invariably, the minister controls the quality and number of staff in the Commission. The minister holds *de facto* power with regards to staffing and remuneration of the Commission. The Act does not provide a comparable standard for the remuneration of staff but leaves it to the discretion of the minister who might simply apply civil service rates.

It is appropriate to note that the staffing provisions in the Act is scanty and does not pre-empt the kind of structure the organisation would have. This is left to the board or even the minister to decide. Secondly, it is quite strange that the Act failed to make concrete provisions for the position of an actuary which is very crucial to the effective performance of the supervisory functions of the Commission. An actuary is essential for the effective determination of capital adequacy, risk profiling and risk management of the Commission. The alternative of securing the appointment of a consultant is quite disappointing because the duty of an actuary is directly linked with the surveillance functions of the Commission. Therefore, at least one actuary must be in-house who probably is supported by consultants.

In summary, the provisions of the Act for resources seem inadequate for effective administration of the insurance sector. The overbearing influence of the minister on

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<sup>67</sup> Ironically, this is only provision relating to supervisory cost.

the resources of the Commission would hinder and compromise the level of supervisory effectiveness. The resource structure needs to be amended in a way that the needs of the Commission determine the budget and not the other way round. The inadequacy of the Commission is confirmed in reports that the Commission had only 20 technically qualified staff out of 153 on its payroll<sup>68</sup> in a period when there were over 100 insurance firms. Evidence also suggests that the Commission does not have actuaries since the employment of at least one actuary has been one of the priorities of the Commission for two years on<sup>69</sup>.

Large amounts of information both financial and technical are required to be submitted to the Commission therefore, it is imperative that the Commission has competent staff to generate a good statistical database. It is utterly unacceptable for an agency which is going to manage a liberalising insurance sector to be understaffed. The Commission requires competent staff for effective surveillance, analysis and management of the NII risks as required under the prudential requirements of the IAIS<sup>70</sup>. This would afford proper planning for the NII and help the risk management process of identifying, analysing and managing the risks of the industry as required by IAIS under the Prudential Requirements of the ICPs<sup>71</sup>.

An alternative regulatory strategy might be for the regulator to adopt a ‘learn by doing’ strategy. This would involve partial market opening and allowing the agency

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<sup>68</sup> Omobola Tolu-Kusimo, ‘Daniel Reappointed Commissioner of Insurance’, *National Mirror Newspaper* (Lagos, 18<sup>th</sup> August 2011), ><http://nationalmirroronline.net/business/business-and-finance/18676.html>> accessed 29<sup>th</sup> August 2011; Oladele Ayeleso, ‘NAICOM Restructures, Consolidates MDRI’ *Nigerian Tribune* (Ibadan, 8<sup>th</sup> June 2011) < <http://www.tribune.com.ng/index.php/insurance/23179-naicom-restructures-consolidates-mdri>> accessed 29<sup>th</sup> August 2011.

<sup>69</sup> Ibid; survey data reveals that no actuary has been employed till date.

<sup>70</sup> IAIS, Insurance Core Principles 18-23.

<sup>71</sup> IAIS ICPs 18-23.

learn while meeting the challenges as they occur. However, this thesis argues that a moderate standard of regulatory infrastructure need to be in place for disastrous circumstances not to result from the experiment. Considering the fact that there would be information asymmetry<sup>72</sup> between foreign suppliers from more developed regulatory system and regulators in developing countries, this may lead to regulatory failure. It is important that experienced staff with good impact assessment skills are in place to avoid chaos. Risk identification and assessment in terms of likelihood of occurrence and the possible severity of the impact is necessary. If impact assessment is inadequate, little may be learnt. Therefore, minimum standards of surveillance need to be in place to enable the regulator identify and assess the impact of any risk and properly develop policy and regulatory options before calamitous effects take place. Consequently, it would be safe to have reforms put in place skilled staff, proper surveillance and risk assessment mechanisms before further opening of the NII. Once this is in place, 'learn by doing' may become a reasonable option for resolving future problems of regulatory incapacities.

Be that as it may, the Act makes provision for the legal protection for officers or representatives of the commission. It is an offence for anyone to partake in the wilful obstruction, interference, assault or the resisting of an officer representing the Commission in the performance of its duties under the Act. There are sanctions in form of fines or prison sentence for offenders<sup>73</sup>. The Act also prohibits the commencement of action against the Commission without giving a 30days notice of intention to commence action containing the details of action

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<sup>72</sup> Cento Veljanovski, 'Strategic Use of Regulation' in Robert Baldwin, Martin Cave and Martin Lodge (eds), *The Oxford Handbook of Regulation* (OUP 2010) 94.

<sup>73</sup> NAICOM Act 1997 s50&59.

From the above analysis, there is need for reforms in the funding provisions to facilitate effective supervision and liberalisation. This would involve opening up the market to foreign insurance providers which may be large conglomerates. Without effective and efficiently qualified staff with wide experience and skills in regulations and supervision, controlling foreign firms may be a mirage. Without effective supervision, liberalisation may not deliver the gains of economic development as expected but may lead to adverse economic effects.

### **Independence and Accountability**

The NAICOM Act makes significant provisions for appointment and removal of members of the board and the funding structure of the Commission as noted earlier. However, there seem to be some provisions affecting the requirements for independence and accountability of the NAICOM.

The Act undermines the independence of the Commission with regards to provisions relating to enforcement of regulatory sanctions, determining the expenditure structure, and the remuneration of staff of the Commission. The provisions of the NAICOM Act do not support institutional, supervisory and budgetary independence<sup>74</sup> of the NAICOM. The commission's regulatory independence is the only form of independence assured under the Act. The pitfall with lack of budgetary independence is that the budget may be inadequate to attract qualified personnel and pay salary that is comparable in the financial services sector<sup>75</sup>. Nevertheless, it is pertinent to note that the Act's provisions for the minister's oversight functions are necessary in some

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<sup>74</sup> See chapter two s4 (c)(vi); Mar Quintyn and Michael W Taylor, 'Regulatory and Supervisory Independence and Financial Stability', IMF WP/02/46, 14

<<http://www.imf.org/external/pubs/cat/longres.aspx?sk=15679.0>> accessed 23rd April 2011.

<sup>75</sup> Quintyn and Taylor (n74)21.

administrative activities. However, where it encroaches into ordinary supervisory functions of the Commission, it has serious implications for the credibility of the agency. It means the Commission is not free from political influence. NAICOM Act also failed to inject effective public accountability into the supervisory process. The Act has specific provisions that make the Commission accountable to its supervisory ministry as analysed earlier under powers of the Commission. They are very few provisions in the NAICOM to hold the Commission accountable to the public<sup>76</sup>. Accountability is a corollary of transparency and together they build confidence and good governance<sup>77</sup>. Lack of independence may result in poor public sector governance occasioning poor supervisory governance<sup>78</sup>. Accountability is an obligation to give reckoning or explanation for one's actions especially in a position of responsibility<sup>79</sup>. In order to fulfil the requirements of accountability, regulators 'need to provide public oversight'; 'maintain and enhance legitimacy'; 'enhance agency governance'; and 'improve agency performance'<sup>80</sup>. In doing this, the agency would be able to build up credibility through public opinion on reputation which is achieved by rules allowing the actions of the agency to be subjected to review<sup>81</sup>. There are no legal provisions ensuring these requirements therefore the credibility and legitimacy of NAICOM is compromised.

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<sup>76</sup> See (n82) & (n83).

<sup>77</sup> Christine Kaufman and Rolf H. Webber, 'The Role of Transparency in Financial Regulation' (2010) 13 JIEL 779.

<sup>78</sup> See chapter two (n192).

<sup>79</sup> Eva Hüpkes, Marc Quintyn, and Michael W. Taylor, 'The Accountability of Financial Sector Supervisors: Principles and Practice' IMF Working Paper WP/05/51, 5.

<sup>80</sup> *ibid* 5-9.

<sup>81</sup> *ibid* 8.

These provisions have dire consequences for liberalisation because it affects the integrity and ultimately the degree of regulatory effectiveness of NAICOM. Without effective supervision, market credibility is at risk and this cannot support liberalisation. Reforms would be required for greater degree of independence and accountability for NAICOM. This will enhance the potential for growth from the liberalisation of the NII.

## 6.5 SUPERVISORY PROCESS

### Transparency

In the NAICOM Act, there are very few provisions that can enhance the transparency of the supervisory process. There is no provision requiring the public knowledge or consultations with the public in the process. There is equally no provision that requires proposed regulations of the Commission to be available for public scrutiny. In the same vein the only avenue provided for interaction of the public with the NAICOM is the public complaints bureau. However, there is no provision to the effect that the activities of the bureau should be made public. Nonetheless, the Act listed publication for sale of annual reports and statistics on insurance industry as one of the functions of the NAICOM<sup>82</sup>. It also mandates the Commission to publish within a reasonable time any information concerning or affecting the insurance industry<sup>83</sup>.

Given that insurance is widely criticised for lack of transparency<sup>84</sup>, this is one area of supervision that needs to be emphasised. There should be provisions in the law

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<sup>82</sup> NAICOM Act 1997 s7 (i).

<sup>83</sup> *ibid* s49 (2).

<sup>84</sup> Terri M. Vaughan, 'Financial Stability and Insurance Supervision: The Future of Prudential Supervision' (2004) 29 GPRI 258, 269.

compelling the Commission to make available for scrutiny the guidelines and other regulations before and after they are made. There is no provision compelling the NAICOM to publish reports of erring insurance firms and details of their sanctions. This has prompted the assertion that the Commission shields insurance companies from the public eye<sup>85</sup>. In response it was reported that NAICOM's representative said that 'the Commission took a less combative approach to regulatory actions despite the temptations to copy other regulators in taking "earth-shaking decisions. We have treated apparent criminal breaches as mere infractions quietly'<sup>86</sup>. This obviously confirms the lack of transparency in NAICOM's supervisory activities. It is a consequence of the failure of the NAICOM Act to make the Commission accountable to the public which it has a moral duty towards. Lack of transparency encourages unethical practices which cannot be accommodated under a liberalised NII. It is imperative that the NAICOM Act should be reformed to have more disclosure regulations and promote better transparency of the supervisory process.

## Cooperation

The NAICOM Act has no provision for cooperation with other relevant agencies whether within or outside the country and this has consequences especially for liberalisation. The reason being that liberalisation may open up the industry to foreign firms which might include conglomerates. Without adequate cooperation with other regulators in the financial sector and regulators in the home countries of these

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<sup>85</sup> Joshua Nse, 'Operators Blame Indiscipline in the Industry on Regulator's Laxity' *The Guardian, Nigeria* (Lagos, 19<sup>th</sup> September 2011) < [http://www.nguardiannews.com/index.php?option=com\\_content&view=article&id=61474:operators-blame-indiscipline-in-industry-on-regulators-laxity&catid=82:insurance&Itemid=588](http://www.nguardiannews.com/index.php?option=com_content&view=article&id=61474:operators-blame-indiscipline-in-industry-on-regulators-laxity&catid=82:insurance&Itemid=588)> accessed 20<sup>th</sup> September 2011.

<sup>86</sup> *ibid*; the regulator being referred to was the CBN that had made public the list of failing banks in Nigeria.

conglomerates, it might be difficult to effectively managed firms with internationalised activities. Reforms will therefore be required to make legal provisions necessitating supervisory cooperation in the Commission.

## Surveillance

The surveillance activities of the Commission are facilitated by powers to inspect, to do actuarial investigation and to intervene. The Act provides for the establishment of an Inspectorate Department<sup>87</sup> which consists of a Chief Inspector of Insurance with a minimum rank of a Director to be assisted by and a number of officers to be known as inspectors as may be deemed necessary by the Commission. Their functions include the inspection, examination or investigation of all insurance institutions at least once every two years<sup>88</sup> and making half yearly reports to the Minister of these activities<sup>89</sup>.

Inspectors in carrying out this function have right of access to all books, accounts and documents, check all registers as required by Act, correspondences, accounting books and verify the legality of all transactions and the investment of capital and statutory reserves of the insurance institution<sup>90</sup>. Wilful or negligent refusal to produce such books as may be required by the inspectors attracts a fine for the insurance institution concerned<sup>91</sup>. Upon completion of the inspection exercise, the inspectors are required to submit a report and recommendations to the Commissioner of Insurance who forwards a copy to the insurance institution in question. The insurance institution or partners has within 14days to submit to the board of directors of the Commission its

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<sup>87</sup> NAICOM Act 1997 s31(1)

<sup>88</sup> *ibid* s31(1)(a).

<sup>89</sup> *ibid* s31(1)(b).

<sup>90</sup> *ibid* s32.

<sup>91</sup> *ibid* s33.

reaction to the report and proposal on how to implement the recommendations of the report. Failure to do so will also attract a daily fine for every day in default and if this persists for more than 60days, the commission may in addition suspend the registration of such an insurance institution<sup>92</sup>.

The Commissioner with the approval of its board may order special inspection or investigation of an insurance institution in the interest of the public, if a director or a policy-holder of the insurance institution makes an application thereof or if the assets of the insurance institution is not sufficient to cover its liabilities or if the insurance company has contravened any of the regulations<sup>93</sup>.

The commission has the duty to appoint actuaries or secure the services of actuarial consultants to investigate the financial conditions of insurance institutions every five (5) years using applicable valuation regulations and submit reports to the commission<sup>94</sup>. The Act also provides powers of intervention in the affairs of any insurance institution in four situations:

- ❖ where it is desirable to do so to protect current and potential policyholders from the inability of the insurance institution to meet its liabilities;
- ❖ where it appears to the Commission that the insurance institution has failed to satisfy its obligations under the Decree;
- ❖ where it appears to the Commission that the insurance institution has furnished misleading or inaccurate information to the Commission; and

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<sup>92</sup> s34

<sup>93</sup> s35(1).

<sup>94</sup> (s36).

- ❖ where other conditions exist that makes it necessary for the Commission to intervene.

These provisions show that are there statutory provisions for surveillance imbedded in the Act however, the frequency, mode and reach of these structures make them inadequate for liberalisation. The Act does provide for market analysis which as the survey revealed focusses on domestic data and little attention is paid to international data analysis which is germane for liberalisation. Besides, a requirement of a frequency of at least once in two years or five years for actuarial investigation is ineffective in ensuring proper surveillance of insurance firms and their activities. Similarly, no reference is made to the risk portfolio as a determinant of the amount of supervisory time and resources to be devoted to individual firms for the purpose of regulatory efficiency and effectiveness<sup>95</sup>. Furthermore, there needs to be regulations emphasising the need for NAICOM to ensure financial stability, competitiveness and viability of the insurance market both as an objective and function of the supervisory agency. The goal of surveillance is to prevent systemic and other risks from occurring in the market. The role of NAICOM should be wide-ranging including effective supervision, policing, surveillance and enforcement. The viability of the insurance market is important for development, growth and even liberalisation. Therefore, reforms would be needed first to include risk based supervision in the activities of the supervisory agency and increase the frequency of monitoring and supervision on insurers with high risk portfolios or with dimming fortunes. Furthermore, surveillance mechanisms should also pay attention to data from the international scene especially to keep abreast of global financial crises and putting in place shock mechanisms for

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<sup>95</sup> See chapter for discussion on regulatory efficiency and effectiveness.

the industry. This is necessary because liberalisation may bring in foreign insurers from jurisdictions with more developed regulatory and surveillance mechanisms who may take advantage of ineffective surveillance in the market to engage in activities that may compromise the stability of the industry.

## **6.6 CONCLUSION**

This chapter has analysed the institutional framework of the NII and benchmarked it against the institutional and supervisory parameters of insurance liberalisation highlighted in chapter four. It is argued that NAICOM as constituted possesses neither the requisite human and financial resources nor the independence necessary for regulating and supervising a liberalised insurance sector.

There is need for institutional reforms in supervision of the NII for an independent, effective and adequately funded supervisory authority devoid of any form of influence whether economic or political. The supervisory structure needs to be transformed prior to the liberalisation of the NII to be able to implement competition and principle based policies. It must also be sensitive to the need for continuous development of the NII within the domestic and international sphere.

There is also need to reform the institutional provisions on the frequency, mode and breadth of surveillance to include analysis of international data which will help prevent unnecessary contagion effect from some global crisis. Emphasis should be on risk based supervision, for regulatory efficiency and effectiveness and activities of the agency needs to be proportional to the risks which are being prevented.

This thesis advocates adequate supervisory cooperation and resource sharing through the adoption of Bi-Polar model supervisory structure<sup>96</sup> which splits financial sector supervision into two one for the deposit taking institutions like banks and another for non-deposit taking sectors like insurance and securities and exchange. The non-deposit taking supervisory agency will pool resources together from existing individual supervisors in the insurance, capital market and securities sectors to build a strong supervisory agency. Resource sharing in the new agency would reduce the current supervisory inadequacies of the NII like understaffing, lack of essential skills and inadequate resources. Each sector would have a director sit on the board of the new supervisory agency which would be funded by the levies from supervised firms and have budgetary independence. The major goal of the agency would be to implement the competition and liberalisation policy of government and take corrective action for defaulters. Supervision should emphasise transparent and efficient operation of the NII putting public interest ahead of all other interests and adapting the NII to domestic and international financial climate. On the whole there should be regulatory efficiency through prudential and risk based regulatory and supervisory policies.

The next chapter analyses the responses from the socio-legal research conducted data from which complements the doctrinal analysis of the legislation in the last two chapters.

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<sup>96</sup> See discussion of various models of supervisory bodies in chapter two s2.4.

## **CHAPTER SEVEN**

### **DATA ANALYSIS AND INTERPRETATION**

#### **7. INTRODUCTION**

The last chapter benchmarked the institutional model of reforms against the institutional provisions of the NAICOM Act of 1997 and concluded with the institutional challenges against the liberalisation of NII. This chapter presents the findings from the Socio-legal exploratory survey<sup>1</sup> conducted on a cross section of stakeholders in the NII to explore and enable an understanding of the regulatory environment of the NII and to complement the doctrinal analysis. A sample size of 10 as argued earlier is sufficient because of the exploratory nature of the survey which does not require representativeness. It is used for the purpose of better understanding the NII regulations and its administration as a result of the fact that legal research and theory is non-existent in this area. It therefore generated insights into some regulatory policies and practices which would not have been evident from the analysis of the legal framework of the NII<sup>2</sup>. Furthermore, the aim of this research is primarily to advocate for unilateral liberalisation for the purpose of restructuring the NII for efficiency, competition and growth prior to taking further binding commitments in the GATS. This survey therefore was aimed at gaining insight into the practices within NAICOM and opinions of other stakeholders within the industry whose actions may have a bearing on the effectiveness of reforms being proposed. Therefore, surveying

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<sup>1</sup> As noted earlier in the introduction, this study is a multi-method research which uses both doctrinal and social science survey research techniques. All the previous six chapters employed the doctrinal technique.

<sup>2</sup> For example, the doctrinal analysis couldn't have revealed the silent embargo placed on licensing of firms which was gotten from this survey.

outside Nigeria would not serve the purpose of the survey. However, the Insurance Model and Best Practices as earlier discussed<sup>3</sup> represent the opinion of foreign suppliers in terms of their expectations for a liberalised insurance market.

Nonetheless, the survey achieved its purpose and the analysis of the result is presented below in three sections. The first focusses on the demographic characteristics of the respondents while the critical analysis and interpretation of data from the survey is presented in the second section. The last section contains the conclusion which distinguishes the aspects of the empirical findings that support the doctrinal analysis and that which does not while explaining the possible reasons for the contradiction.

### **7.1. BASIC DEMOGRAPHIC CHARACTERISTICS OF THE SAMPLE**

There are fifty nine (59) insurance companies in the NII and 702 insurance brokerage firms however, the total number of insurance policyholders is unknown because there is no database for such. Nonetheless, the sample included insurance executives, NAICOM representative, insurance brokers and policyholders. In terms of representativeness, this sample had about 10% of all insurance chief executives and about 2% of insurance brokers while the level of representativeness of policy holders cannot be easily determined. As stated earlier, insurance executives are pivotal to effective regulation and supervision of insurance service since they constitute an important interest group in debates relating to liberalisation and trade in insurance services<sup>4</sup>. Therefore, their opinion on regulatory and supervisory practices is

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<sup>3</sup> See discussion of Insurance Model and Best Practices in s4.2.

<sup>4</sup> Insurance executives greatly influences the trade policies of their government with regards to their

significant to the understanding of the legal framework of the in the NII.

### **7.1.1 Gender and Age:**

All the respondents were male and 70% of them were in the 50-55yrs age bracket<sup>5</sup>, 20% in the 40-45yrs and 10% in the 45-50yrs age bracket. This implies that most of the respondents were above 50years.

### **7.1.2 Occupation**

Half of the respondents were insurance executives, 20% insurance brokers, 20% policyholders and 10% insurance regulator. About 90% of our respondents held senior executive positions while only 10% was in the middle management cadre. However, 80% of them were engaged in the Nigerian insurance industry while 20% worked in other sectors of the economy. Therefore, most of the respondents were senior executives in the insurance industry.

### **7.1.3 Educational Qualification**

About 40% of the respondents were lawyers<sup>6</sup>, 40% had degrees in the social sciences and humanities, while 20% were higher diploma holders. This is significant because 80% of the respondents had a minimum of a university degree. This implies that most the respondent were educated.

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sector as evidenced in US and UK insurers lobbying during the process of China's liberalisation of its insurance sector; Stephen P. D'Arcy and Hui Xia, 'Insurance and China's Entry into WTO' (2003) 6 Risk Management and Insurance Review 7, 18.

<sup>5</sup> Using the criteria of interviewing senior executives of insurance firm, I discovered these executives were in the age bracket of 40-55yrs.

<sup>6</sup> Though only half of these were in practice

## **7.2 ANALYSIS AND INTERPRETATION OF SURVEY DATA**

A critical analysis of the data gathered from the research instrument is presented below.

### **7.2.1 IAIS Insurance Core Principles**

This section analyses responses on the IAIS core principles on insurance supervision. The significance of the principles is that they are standards of insurance regulation and supervision. These principles were also used in the construction of the parameters for insurance liberalisation. The grouping of the responses follows that of the original IAIS document.

#### **7.2.1.1 Conditions for Effective Insurance Supervision**

The questions in this section were pertaining to the policy, economic and legal environment of NAICOM. Responses revealed that 90% of respondents agreed that NAICOM relies on a strong policy, institutional and legal framework citing the IA and NAICOM Act as providing adequate policy guide, legal and institutional framework. When asked what the policies were, responses included NEPAD<sup>7</sup> and Local Content Policy<sup>8</sup> and market development<sup>9</sup> while the NAICOM respondent however was the only one who stated consumer protection as the overall policy of NAICOM. Nevertheless, 80% of the respondents were of the opinion that the financial market within which NAICOM existed is not well developed. Reasons adduced include underdeveloped micro elements of the economy and the fact that Nigeria was a developing nation. The remaining 20% were of the opinion that the Nigerian financial market was either developed or developing.

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<sup>7</sup> See chapter one (n93).

<sup>8</sup> This is the Oil and Gas Industry Content Development Act of 2010.

<sup>9</sup> This means Market Development and Restructuring Initiatives(MDRI).

The significance of these responses is that the overall policy focus of the NAICOM is not clear to all stakeholders<sup>10</sup> and the Nigerian financial sector is still underdeveloped. Therefore, without a clear policy and a developed financial market structure NAICOM clearly lacks one of the basic requirements for effective supervision and by implication successful liberalisation of the insurance sector. Relevant laws in the NII need to provide a clear policy focus which the governing board of NAICOM should pursue. The main goal of insurance services regulation is consumer protection. This goal needs to be reflected as an overriding policy of NAICOM. The preservation of an efficient and competitive market is a policy that also needs to be clearly emphasised in the operations of the Commission. These are fundamental policies that insurance supervisory bodies need to adopt.<sup>11</sup> There is need to strengthen the financial environment with reforms that would develop the market to world standards. The reforms in the policy focus of NAICOM and the financial environment of the NII would offer a better platform for the liberalisation of the NII.

#### **7.2.1.2 The Supervisory System**

The questions asked in this section are associated to the institutional framework of the NAICOM focussing on objectives, adequacy of powers and resources, transparency and accountability, independence and cooperation with other financial service regulators.

Responses on the supervisory objectives of NAICOM revealed that the objectives were clearly defined since only 80% of the respondents actually believe they are clear

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<sup>10</sup> The situation may be worse with the public in general.

<sup>11</sup> IAIS, 'Insurance Core Principles and Methodology' (2003) 6

<[http://www.iaisweb.org/temp/Insurance\\_core\\_principles\\_and\\_methodology.pdf](http://www.iaisweb.org/temp/Insurance_core_principles_and_methodology.pdf)> accessed 9<sup>th</sup> October 2009.

while 20% had contrary opinion.

The responses on the adequacy of powers of NAICOM were split equally. Some respondent cited the NAICOM Act as limiting the powers of the Commission by requiring approval from the minister to sanction erring insurance firms. Insurance company executives constituted the majority of the respondents that stated that the Commission's powers were adequate. They revealed that the adequacy of the powers of the Commission had become apparent with the appointment of the new commissioner. They noted an increase in number and content of operational guidelines issued, detailed scrutiny of insurance companies' activities and increasing number of sanctions awarded. From the responses, it can be implied that the Commission has moderate supervisory powers. However, to effect a successful liberalisation of the NII, the NAICOM needs to be shielded from the influence of government. This can be made possible only by reforming that part of the law.

All the respondents agreed that NAICOM had enough legal protection as provided for all public officers<sup>12</sup> but were divided on the adequacy of the commission's financial resources. A total of 60% were of the opinion that the Commission had inadequate financial resources<sup>13</sup>. They noted that the Commission's budget was tied to the ministry being a government agency they were thus underfunded<sup>14</sup>. However, 30% disagreed stating that the Commission's income was not limited to the budget alone. They stated that financial resources should be adequate with the 1% levy on earnings of insurance firms together with income from fees paid for renewals, registration and

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<sup>12</sup> Public Officer's Protection Act LFN 1990.

<sup>13</sup> Amongst them was the respondent from NAICOM.

<sup>14</sup> Poor working environment of the staff is cited as one of the evidences of underfunding.

penalties. The remaining 10% of the respondents had no idea about the Commission's finances. The responses revealed a general belief in the inadequacy of the financial resources of the commission. However, it is important to note that NAICOM's reports for 2010 revealed a gross premium of about N158billion for the entire NII<sup>15</sup> which is a little over \$1billion. Calculating the 1% received by NAICOM gives N1.58billion i.e. about \$150million as levies alone. This is a considerably huge amount of money by Nigerian standards which makes it challenging to imagine that NAICOM is underfunded<sup>16</sup>. However, when juxtaposed with the analysis of the institutional provisions in chapter six, it would give a logical reason for accepting the opinion of majority of the respondents about the inadequacy of the funds at NAICOM's disposal. The respondents who believed otherwise may not be aware of the expenditure constraints of the Commission<sup>17</sup>. This thesis reiterates that inadequate funding of the supervisory agency impacts negatively on its operations and on regulatory effectiveness in particular which is required to facilitate successful liberalisation of the NII.

Responses to the question on the level of independence and accountability of NAICOM revealed that NAICOM is not independent but accountable only to the Ministry of Finance and not to the public or the consumers of insurance services citing the law (i.e. IA and NAICOM Act)<sup>18</sup>. This confirmed the conclusions drawn earlier in chapter five. Independence, accountability and integrity are corollaries that

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<sup>15</sup> NAICOM, 'Home' <<http://www.naicom.gov.ng/Index.php?p=Home>> accessed 11<sup>th</sup> March 2011.

<sup>16</sup> However, offices of NAICOM visited during the interviews were in very bad state needing renovation and lacking adequate tools for running an office. This is not surprising since most government offices in Nigeria wear such looks therefore it would be impossible to make categorical statements based on the state of the office.

<sup>17</sup> Whereby only 50% of their income could be expended on operational costs See discussion on supervisory authority in chapter 6 s6.1.2

<sup>18</sup> All the respondents agreed

are vital for liberalisation. A regulatory agency without credibility cannot supervise a liberalised insurance market bearing in mind its negative consequences. This thesis posits that the NAICOM is not independent and reforms geared towards strengthening its independence in all dimensions are required.

Responses to questions on the supervisory process revealed that NAICOM was not transparent because most of the activities of NAICOM are not known to the public. Policyholders and the public in general are not informed about the activities of the Commission. Only 20% of the respondents believed otherwise stating that NAICOM is as transparent as provided by the law. They were of the opinion that revealing too much of the activities may exacerbate the existing lack of trust between the public and insurance companies<sup>19</sup>. This has significance for liberalisation because transparency is a central principle of the WTO/GATS model. A liberalised insurance sector requires transparency so that foreign suppliers are aware of the real market situations. This thesis posits that lack of transparency will not reduce the trust issues but worsen them. This confirms the need to reform the legislative and institutional framework of the NII to reflect the principles of transparency. Reforms anticipated will facilitate greater openness and successful liberalisation of the sector.

The responses power to hire, train and retrain as also revealed that NAICOM had adequate powers with the recent recruitment exercise of NAICOM as proof. However, only 20% had contrary opinion<sup>20</sup> stating that as an agency of government,

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<sup>19</sup> As noted in earlier chapters, insurance is a trust business but there is overwhelming lack of trust for insurance companies in Nigeria therefore, majority of the Nigerian population which ought to buy insurance do not as a result.

<sup>20</sup> The respondent from NAICOM revealed there is still staff inadequacy warranting the use of consultants for inspection and research activities of the Commission.

the Commission's recruitment is tied to that of the public service and therefore, the human capital needs of the Commission are not adequately. This was stated to be the consequence of inadequate financial resources. However, when juxtaposed with the analysis in chapter five, mandatory approval of the remuneration and conditions of service may present some constraints to the exercise of this power. Nonetheless, it is significant to note that for a liberalised NII require an adequately staff supervisory agency.

The survey also revealed that NAICOM engages in consultations with stakeholders and allows feedback but remains accountable only to its governing board and Minister of Finance. It was also revealed that though a number of NAICOM's activities are published on their website but most Nigerians lack access to the internet. This further confirms the lack of transparency in NAICOM's activities. Information that is not accessible is technically unavailable in law. Liberalisation requires not only availability but accessibility of information to enable policyholders and even investors make informed decisions about the market. NAICOM needs to strengthen its information regulations and make available through the print and other electronic media laws and guidelines for greater accessibility to the public.

Respondents also confirmed that NAICOM cooperates with other supervisory agencies in the financial sector being a member of the Financial Services Coordinating Committee (FSCC)<sup>21</sup>. However there was doubt about the effectiveness the cooperation due lack of trust among the regulators. It was noted that information

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<sup>21</sup> This is a body set up by the Central Bank of Nigeria(CBN) in 1994 to facilitate a formal framework for coordination of the supervisory and regulatory activities in Nigeria through inter-agency consultations and meetings. Members of this body include CBN, NAICOM, Corporate Affairs Commission (CAC) and the Federal Ministry of Finance.

revealed about the pensions business led to its separation from other insurance services. However, it is important to note that 30% of the respondents were not aware of any cooperation while 10% felt no cooperation exists. From the responses one can conclude that the NAICOM cooperates with other financial regulators but in an atmosphere of doubt.

In summary, the above analysis has revealed that NAICOM has clear supervisory objectives defined by the law. The commission also has power of supervision, hiring and training staff though the overbearing influence from the government ministry on these activities is noted. NAICOM's financial resources are inadequate not because there are inadequate sources of funds but probably because of provisions of the NAICOM Act allowing only 50% for operational matters. Nonetheless, financial independence from the ministry would be desirable. This would reduce the effect of political influence regulatory activities. Moreover, the supervisory process is not transparent though consultations are held with stakeholders before policy decisions are made. The Commission has the moral responsibility to provide full and up to date information about the insurance market to all categories of people that may be interested such as stakeholders and the public at large. Finally, the level of supervisory cooperation does inspire information sharing or inter-agency supervision. This affects NAICOM's group wide supervision<sup>22</sup> functions. Reforms in the institutional provisions in the law are required to strengthen the independence, accountability and credibility of the NAICOM for successful liberalisation of the NII. This may involve adopting one of the earlier models suggested in chapter two<sup>23</sup>.

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<sup>22</sup> As would be revealed in later in this chapter.

<sup>23</sup> These models are discussed in chapter two s2.5.

### 7.2.1.3 The Supervised Entity

This subsection asked questions relating to the licensing and supervision of insurance firms within Nigeria.

Responses to questions on the licensing process in Nigeria revealed that it is clearly stated in the law<sup>24</sup> and that the qualification and technical requirements were very objective. However, it was confirmed by 60% of the respondents that the process was not public. This has significant implications for transparency and liberalisation as noted above in s7.2.1.2. Equally important is the revelation that there is an embargo on licensing of new insurance companies. Clearly, placing an embargo on licensing would be counterproductive for liberalisation because the market needs competition for effective liberalisation. This thesis posits that the embargo on licensing needs to be lifted for effective and successful liberalisation to take place.

The analysis of responses also revealed that the IA and CAMA ensure the suitability of owners and managers of insurance firms. The corporate governance requirements<sup>25</sup> of NAICOM for anyone aspiring to acquire or manage insurance firms also ensure that only fit and proper person are involved in the sector. However, 20% were of the opinion that some unfit people do sometimes find their way into the leadership of insurance firms without being noticed. This claim could not be substantiated. This finding is pertinent with regards to the liberalisation of the NII. It promotes a healthy market in which liberalisation will thrive.

All the respondents agreed that NAICOM's approval was required to effect a change

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<sup>24</sup> They all referred to the appropriate sections of the IA 2003

<sup>25</sup> This includes clearance from police and EFCC (Economic and Financial Crimes Commission).

in control or portfolio transfer of insurance firms as dictated by law<sup>26</sup>. However, it was noted by 50% of the respondents that quite a lot of small fragment transfers go unnoticed because the law only requires NAICOM to be notified when the amount changed or transferred is up to 25% of the company's equity. This response revealed that the law concerning change of control or ownership is not firm enough and there is need to look at the identified loophole through serial accumulation of interests in insurance companies. This is crucial to ensure that only suitable people are involved in the management and ownership of insurance companies.

Responses on the corporate governance issues revealed that 90% of the respondents are aware that the rights of all parties of interest were protected under the Code of Corporate Governance issued by NAICOM and the board was the focal point of the governance system. Almost all the respondents were familiar with the code confirming that measures of corporate discipline, transparency, accountability, fairness were addressed by the code but that social responsibility was not emphasized. One respondent however was of the opinion that the rights of shareholders was not as adequately provided for as those of the consumers. The responses have significant implications for liberalisation because it confirms that the NII corporate governance code is in line with the standards of international organisations. This is a measure of member's conformity to obligations in the GATS.

Disappointingly, the responses revealed that most insurance companies in the NII lacked internal control systems. A total of 90% of the respondents confirmed that it was a new system that NAICOM had introduced with the Code of Corporate

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<sup>26</sup> Insurance Act 2003 s30-1.

Governance<sup>27</sup>. The implications of not having internal control systems are that there would not be effective risk management and this makes insurance firms vulnerable. It is therefore significant that internal control systems are in place to promote sound and healthy firm for liberalisation.

#### **7.2.1.4 On-going Supervision**

This subsection had questions relating to the supervisory function of NAICOM specifically the continuous monitoring, sanctioning and analysis of the Nigerian insurance market.

Majority of the responses confirm that NAICOM monitors, evaluates and performs on-site inspection the insurance market though sometimes through consultants. Only, 30% of the respondents believed that proper market analysis was not done considering the fact that a number of long standing market problems still persists and are not addressed<sup>28</sup>. It was also confirmed by 90% of the respondents that NAICOM receives enough information to do off-site monitoring and evaluation of the market. Doubts were nonetheless raised about the use to which the information was put.

It is commendable that the Commission does onsite and offsite inspection because these are measures which help identify market problems. However, it is equally important that the information is put to use especially during the offsite inspection which assists in identifying potential problems in between on-site inspections. These are systems that would be valuable for liberalisation in managing large multinational

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<sup>27</sup> *ibid* s9;

<sup>28</sup> Some of the problems listed include unethical practices of rate cutting, impact of the Nigerian Stock Exchange crisis on the capital of insurance firms and growing liquidity resulting from it.

that may establish commercial presence in Nigeria. Therefore, it is imperative that NAICOM develop programmes that can assist in generating data that would identify problems to order to avoid the possibility of systemic risk.

Furthermore, the responses reveal that NAICOM is reactionary and it uses guidelines as medium. A total of 60% of the respondents stated that the Commission does more of corrective than preventive action. Meanwhile 30% of the respondents were of the opinion that preventive measures are taken by NAICOM when problems are identified through on-site supervision. This response is relevant to the effectiveness of the NAICOM in performing its oversight function on insurance firms. The inability of the Commission to identify market challenges before they escalate increases the potential for systemic risk. A system of risk identification is very crucial to facilitate a sound insurance market and successful liberalisation. Care must be taken against negative consequences of liberalising without having effective supervisory and legislative regimes in place. This is why it is germane that the Commission has sufficiently qualified staff to support effective performance of its functions.

The survey also revealed that sanctions were enforced but not publicly disclosed by NAICOM. Only 10% of the respondent disagreed with this fact. Of those agreeing, 40% of the respondents noted that publicly disclosed sanctions were politically motivated while 20% were critical of the practice of making companies in pay situations that chief executives are personally liable for. The relevance of this response is that sanctions are enforced and this confirms ability of NAICOM to exercise regulatory authority of insurers in the NII.

Furthermore, responses from 90% of the respondent confirmed the availability of various options for companies' exit under CAMA. This revealed that the respondents were more conversant with the company law in Nigeria than the IA 2003. The provisions for winding up and exit of firms from the market which protect policyholders' interest are also in IA 2003 as analysed in the previous chapter<sup>29</sup>.

On group-wide supervision, all respondents were unanimous in their opinion that NAICOM does supervision only on a solo basis. It was further revealed that group business was not common in Nigeria and the financial reports of insurance companies often reveal the amount of equity held by other companies which by law should not exceed 20% of the total equity.

From the analysis on on-going supervision it is revealed that NAICOM performs all the necessary regulatory functions but it is not effective in all preventive actions or identifying potential risks.

#### **7.2.1.5 Prudential Requirements-**

This subsection enquired about measures taken by the NAICOM to ensure insurance companies are prudent in managing their finances.

Responses by 80% of the respondents revealed that NAICOM does proper management of the risk portfolios of the NII, both on site and off site while others disagreed. This response is strange considering that about half of the respondents had earlier said that the data collected off site is not put to much use. However, all the

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<sup>29</sup> See chapter six s6.2

respondents confirmed that NAICOM ensures that insurance firms do proper risk evaluation and management through reinsurance mainly and the internal control systems put in place but not with the use of any statistical risk analysis tools. It was also confirmed by 80% of the respondents that NAICOM enforces strong compliance to technical standards and provisions for liabilities and also possesses the necessary authority to determine the adequacy of these provisions<sup>30</sup>.

Responses of 80% of the respondents also established that NAICOM ensures compliance with investment standards as provided by the various laws and also issues guidelines to complement these laws. However, 40% of the respondents revealed that the Commission enforces the IA and the Trustee Investment Act which also limits investment in unquoted firms to 10%. All the respondents confirmed that derivatives were not in use in the NFS as a form of investment.

It was also confirmed by 80% of the respondents that capital adequacy and solvency requirements were enforced by the NAICOM using the provisions of the IA and complementary operational guidelines.

The above responses confirm that NAICOM enforce compliance to standards of prudential requirement either provided by law or from its guidelines. However, a more objective form of risk analysis ought to be encouraged in order to meet global standards for the liberalisation of the NII. The essence of an insurance regulatory regime is to ensure solvency of insurance providers. The solvency and capital regimes are therefore paramount in the entire risk management of individual insurers and the

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<sup>30</sup> NAICOM Act was cited as the enabling law.

market as a whole. As noted earlier in chapter five, performance-based regimes cannot support liberalisation. This thesis reiterates again that there is need for reforms in the prudential regulations of the NII to adopt risk based prudential regulation. This would force insurers to do effective risk management and become more prudent in their finance and investment and ultimately make the economic development achievable in Nigeria from the liberalisation of the NII.

#### **7.2.1.6 Market and Consumers**

In this section, questions relating to market conduct and consumer protection were posed to the respondents.

All the respondents agreed that NAICOM directly sets requirements for the conduct of business by intermediaries through annual Operational Guidelines and monitors their compliance through on-site inspections and off-site inspections of reports mandatorily sent to Commission<sup>31</sup>. However, 60% of the respondents believed that NAICOM sets minimum standards for insurers and intermediaries dealing with consumers. These include approving new products and different levels of authorization, avenue for complaints, and arbitration panels and so on. On the other hand, 40% disagreed citing poor pre-contract standards. Furthermore, all the respondents agreed that NAICOM ensures timely disclosure of information through insurance companies' annual accounts is approved by NAICOM before publication for Annual General Meetings. It is important to note that 20%<sup>32</sup> of the respondents stated that stakeholders do not understand financial reports of insurance companies.

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<sup>31</sup> This is a recent development because hitherto, self-regulation policy where supervision was left to National Council of Registered Insurance Brokers. Now what the NCRIB does is certification of its members.

<sup>32</sup> These were the policyholders amongst the respondents.

This is significant because it accounts for the lack of interest in the shares of insurance firms. It is imperative that transparency is emphasised in every aspect of the industry<sup>33</sup>.

Responses to questions on fraud revealed that NAICOM ensure early detection and management of fraud through internal control systems which mandates that officers within the insurance companies have various approval levels. NAICOM ensures that officers at different levels are fit and proper persons having the requisite experience. The Commission also makes the reporting of all frauds by all insurance firms obligatory. Information on the detection and management of fraud are published annually in Operational Guidelines and this involves premium conversion or litigation in some cases.

It is however argued that the internal control systems within insurance firms need to be strengthened. Efforts should be made to ensure that the size of the internal control system is commensurate with the risk portfolios of each insurance company. Considering fact that most insurance companies are just starting to put in place these systems, NAICOM needs to enforce strict compliance with international standards in this regard.

#### **7.2.1.7 Anti-money laundering: Combating the Financing of Terrorism (AML/CFT)**

The survey established that NAICOM partners with the EFCC to ensure that money laundering does not occur in the NII and the Commission's KYC programme. However, 40% of the respondents condemn the lack of commitment on the part of

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<sup>33</sup> See discussion in chapter three on importance of transparency.

insurers and lack of monitoring from the Commission.

In summary, the responses in this subsection revealed that NAICOM has in place measures of controlling intermediaries, protecting consumers, information disclosure, detection and management of fraud, together with anti-money laundering activities within the NII. Conceited effort is required to avoid fraudulent practices of money laundering within the NII to protect consumers. Greater compliance needs to be enforced with regards to fraud and anti-money laundering regulations. The law needs to strengthen consumer rights because that is the primary goal of insurance regulation<sup>34</sup>.

## **7.2.2 Regulatory Principles**

In this section respondents were asked to assess the degree of application of the principles of transparency, local protectionism, reciprocity, proportionality, risk based and independent regulatory authority in the Nigerian insurance law and administration. The options ranged for not used, fairly used and highly used.

### **7.2.2.1 Transparency<sup>35</sup>**

Just 40% of the respondents believed transparency was not being applied, 30% felt it was fairly applied, while the remaining 30% of the respondents believed it was highly applied. Majority of the respondents believed that transparency was applied as a regulatory principle by NAICOM. This is not in consonance with the earlier analysis where majority of the respondents believed the NAICOM was not transparent. In the earlier questions, respondents had related transparency to supervisory activities

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<sup>34</sup> See discussion on goals of insurance in chapter two.

<sup>35</sup> This question treats transparency as a regulatory principles. However, transparency within the context of GATS is treated in s7.4.2.1.

mainly between the regulator and regulated. However, here the focus of respondents seems to be the relationship between the regulator and the public. The respondent being mainly from the industry were not in support of allowing public knowledge of supervisory activities especially with regards the enforcement of penalties against erring insurance firms. Therefore, the responses were based on what the focus of the respondents was. This reveals that the standards of transparency in Nigeria seem to be in parity with global standards. Transparency of an insurance supervisory body is a responsibility which it owes to all including the public. This requires the body to open up its decision making process to the extent required only to preserve commercial confidentiality<sup>36</sup>. However, the Commission applies ‘selective transparency’ i.e. some activities are open while some are not so open. This portrays that the Commission is more interested in protecting insurers than building confidence and competence in the market. However it is pertinent to state at this juncture that insurance regulatory reforms needs to provide adequate information regulations so that the issue of transparency of the Commission can be statutorily addressed<sup>37</sup>.

#### **7.2.2.2 Local Protectionism**

Almost all the respondents believe that local protectionism is highly applied in the regulations of insurance in Nigeria because the law protects domestic providers while shutting out foreign providers. This is significant for liberalisation because the NII needs to be more open and competitive to increase product quality while cutting down

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<sup>36</sup> Mar Quintyn and Michael W Taylor, ‘Regulatory and Supervisory Independence and Financial Stability’, IMF WP/02/46, 33

<<http://www.imf.org/external/pubs/cat/longres.aspx?sk=15679.0>> accessed 23rd April 2011.

<sup>37</sup> Quintyn and Taylor identified three broad types of financial regulations which are economic, prudential and information regulation. While there is not much problem concerning economic regulations which concern pricing of products and entry and exit from the market, the prudential regulations have been discussed under the analysis of the responses on prudential requirements of IAIS.

prices and enhancing growth. This underscores the need for liberalisation.

### **7.2.2.3 Reciprocity**

On reciprocity, all the respondents believed that reciprocity is not applied in Nigerian regulations because foreign insurance company's participation in the country is low. This is not surprising because Nigeria is yet to be properly locked into the WTO/GATS liberalisation model though it has a few commitments. Once real commitments are made in the GATS after substantial reforms leading to liberalisation, reciprocity would ensure that Nigerian insurers would have market access in countries of trading partners.

### **7.2.2.4 Proportionality**

From the survey response, 80% of the respondents believed that proportionality principle was applied to regulations because of the need to sanitize the market. However, 20% were of the opinion that proportionality was not applied because some of the requirements of the law were ridiculous. Some of the examples cited included the code of corporate governance which required members of the board of insurance companies to divulge information about their personal bank details. It was further argued that there was dwindling investment in the NII and these regulations could make it worse. Most importantly, it is asserted that the cost of business is increasing with the quarterly and annual reports requested from insurers. As earlier noted in chapter two, cost benefit analysis is required to ensure that the cost of a regulation is not higher than the benefits to be derived from it<sup>38</sup>.

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<sup>38</sup> See s2.4

### **7.2.2.5 Risk Based Regulation**

All the respondents confirmed that risk based principles were not yet in use in the regulation of insurance business in Nigeria. However, the respondent from NAICOM did state that plans were already in place to adopt the principle<sup>39</sup>.

### **7.2.3 Insurance Model Schedule and Best Practices**

This section analyses responses to questions on the applicability of the NII to the Insurance Model Schedule.

#### **7.2.3.1 Market Access on Cross Border Supply**

All respondents agreed that cross border mode of market access was not available in since local incorporation was compulsory for every provider of insurance in Nigeria<sup>40</sup>. The respondents also confirmed restrictions in form of 5% compulsory cession made to Africa Reinsurance Corporation and need for approval to transact with foreign reinsurers.

#### **7.2.3.2 Market Access for Commercial Presence mode:**

##### **Form of establishment,**

All the respondents stated that a foreign company can set up a subsidiary with 100% ownership either by acquiring an existing company or setting up a new one for as long as the provisions of CAMA are met. However, 60% of the respondent revealed that it had never been done because foreign firms prefer to partner with domestic firms usually in a Joint Venture. It was also gathered from the responses that Foreign Direct Investments (FDI) in the NII was often through the procurement of equity in existing

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<sup>39</sup> The Commissioner of insurance had indicated in September 2010 that the Commission is considering adopting a risk rating model and the two under consideration are the Australian Prudential Regulatory Authority (APRA) and the Office of the Superintendent for Insurance of Canada (OSFI) models. Keynote Address of the Commissioner of Insurance as a seminar of National Insurance Correspondents Held in Calabar, Nigeria 29-30 September 2011. <http://www.naicom.gov.ng/Index.php?p=Home> accessed 15/3/2011

<sup>40</sup> Other 10% was a policyholder and had no idea.

insurance firms. All the respondents also agreed that a foreign insurance supplier can provide the insurance services in Nigerian market using its home company name. However, 20% of respondents were of the opinion that a foreign supplier can be denied access into the Nigerian insurance market because of the legal nature of at home to avoid ‘contagion effect’<sup>41</sup>.

### *Equity Shareholding*

The respondents were unanimous in their belief that the percentage of equity shareholding of the foreign supplier in joint ventures, is determined solely by the parties themselves and not prescribed by any law or regulation. It was also agreed that there exist no Nigerian law prescribing minimum or maximum equity shareholding for foreigners.

### *Compulsory Insurances*

All the respondents were also in agreement about the fact that there are no restrictions to foreign suppliers on compulsory Insurances so long it is locally incorporated.

### *Monopolies*

Majority of the respondents (90%) stated that monopolies do not exist within the Nigerian insurance market though 10% cited the Nigerian Agricultural Insurance Corporation (NAIC) which has monopoly of agricultural insurances in Nigeria<sup>42</sup>. There is no evidence of monopoly despite the mix up by the respondent as to the status of NAIC.

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<sup>41</sup> This means the transmission of financial crisis from one country to another such as a shock in one is linked to those experienced in another like in the Asian Crises.

<sup>42</sup> See discussion on NAIC in chapter five s5.2.

### *Pension Fund Management*

All the respondents confirmed that pensions management was now in private hands since the Pensions Act of 2004 and there was no discrimination for locally incorporated foreign supplier. However, 10% of the respondent did foresee such discrimination once there are foreign entrants into the NII.

#### **7.2.3.3 Market Access for Temporary Entry of Natural Persons:**

A majority (80%) of the respondents stated that there are restrictions on the Market Access for Temporary Entry of Natural Persons in insurance, immigrations law and also the recent local content law<sup>43</sup>. It was interesting to note that 60% of the respondents were unaware that it is illegal to engage a foreign adjuster without an approval from NAICOM. All the respondents affirmed that licensed foreign insurance suppliers are at liberty to choose their representatives but this was also subject to immigration. All the respondents had no idea about the length of time it takes to issue entry visas for foreign professionals so they could not state whether it was prompt or not.

#### **7.2.3.4 National Treatment**

Majority (80%) of the respondents confirmed that discrimination does not exist for locally incorporated foreign firms with regards to competing for insurances of federal government owned enterprises. Nonetheless, state governments favour state owned insurance companies. The same number of respondents also agreed that foreigners are

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<sup>43</sup> See discussion on Immigration Act in chapter five s5.3.2.

not treated less favourably than domestic insurers in capital, solvency, reserves, tax and other financial requirements. With regards to the use of prudential regulations, 80% of the respondents also stated that NAICOM does consult with insurance firms in a continuous dialogue and also has the objectives stated in the regulations and guidelines.

#### **7.2.4 Best Practices under GATS**

This section contains questions relevant to Article XVIII i.e. under Additional Commitments other than those under market access and national treatment. It deals with issues of transparency, solvency, monopolies and the independence of the regulatory authority.

##### **7.2.4.1 Transparency Requirement**

The requirements are public availability of law, public scrutiny of laws before enactment, information setting out and simplifying licensing procedure, procedure for licensing, availability of financial service information, publicly available non-discriminatory rules for handling troubled firms.

Responses from all respondent revealed that all federal laws are made public, published in the Official Gazette and online on the websites of relevant government agency. It was also confirmed that insurance laws and regulations are available on NAICOM's website. Furthermore, all the respondents confirmed that laws are enacted by national assembly and the bill passes through various stages and it include public hearings. However, 40% of the respondents were critical of the process because public hearings are held at short notices in the federal capital. This deprives stakeholders of the ability to attend and make proposals. Furthermore, 80% of the

respondents confirmed that new insurance laws or regulations often allows for a period of grace which often is between one and two years to allow market participants become familiar and take steps to implement them. They cited the proposed adoption of the International financial Reporting Standards (IFRS) standards.

On transparency of licensing process, 80% of the respondents stated that the IA clearly spells out the necessary procedure and required documents though no insurance company has been licensed in recent times. It was further averred that annual guidelines of NAICOM has no established procedure for determining credit worthiness of insurance firms though copies of their annual reports are available at the CAC. Some respondents added that the Nigerian Insurance Association (NIA) and some individual insurance companies belong to independent rating and credit organizations. However, it is the prerogative of these insurance companies to submit to rating agencies without inhibitions. For information on financial services, all respondents stated that the CAC, SEC and CBN all have financial services information on Nigeria and any willing insurance supplier can assess such information from the websites of these agencies. For insurance companies, NIA issues annual reports containing financial service information on their members.

It was however disclosed by 80% of the respondents that on-discriminatory rules and procedures for identification and handling of financially troubled institutions is not available whether publicly or otherwise. Nonetheless, they are aware that the IA does make provisions for identifying troubled insurance firms<sup>44</sup>. None of the respondents could tell if taxation measures affecting insurance were notified the WTO.

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<sup>44</sup> Found no specific provisions for identifying troubled insurance companies in the IA but from

The significance of these findings is that Nigeria is not in strict compliance with the transparency requirements under the GATS model. The country would need to take publication and notification requirements on legislation and rules seriously. This is a fundamental principle in the WTO/GATS framework especially since the attraction of foreign investment is one of the aims of liberalisation. Nonetheless, transparency is vital for the achievement of the objectives of NII liberalisation.

#### **7.2.4.2. Solvency and Prudential Focus**

Majority of respondents (80%) confirmed that the filing and approval for new products with NAICOM<sup>45</sup> is mandatory with fees but it was made free by the waiver in the Operational Guidelines of 2011. Rates of insurance premiums are usually on tariff for compulsory insurance policies and voluntary for other types of insurances. However, it was gathered that there existed a voluntary market agreement to eliminate rate cutting with sanctions imposed for breaching them. The respondents also confirmed that there is no restriction on payment of dividends by foreign insurance companies in any of the laws.

All respondents confirmed Nigeria's adoption of IFRS and 80% confirmed their awareness of NAICOM 2011 guidelines which advised all insurance firms to submit a plan for conversion to this new reporting system<sup>46</sup>. Refreshingly, 80% of the respondent were of the opinion that the NAICOM is in the process of adopting the

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cancellation of registration, solvency, and winding up provisions in the IA one can infer

<sup>45</sup> Insurance Act 2003 s16.

<sup>46</sup> NAICOM Operational Guideline 2011 Para 6.

International Actuarial Standards Association (IASA) standards for the evaluation of the financial strength of insurance companies.

#### **7.2.4.3 Insurance Monopolies**

The responses here were the same as under the Insurance Model Questions. It is pertinent to note that GATS does not prohibit monopolies but require them to maintain separate accounts for monopoly and non-monopoly activities. All the respondents had not information on the accounts of NAIC.

#### **7.2.4.4 Independent Regulatory Authority**

The entire respondents agree that NAICOM was not independent, though they agree that Commission is a government agency, impartial and encourages competition within the NII. This corroborates earlier finding that about the lack of independence of NAICOM. All were also unanimous in their opinion that NAICOM has created a level playing ground for participants allowing for effective competition.

### **7.3 CONCLUSION**

This chapter analysed the responses from the survey research and found that the responses offers insight into the implementation of laws examined in the legal analysis especially the NAICOM Act. There were points of agreement between the doctrinal and survey findings such as the fact that the policy focus of NAICOM was not clear, and the agency lacked adequate powers especially those relating to human and financial resources. Other areas of convergence include the lack of independence and accountability of the Commission and the non-application of regulatory principles

like reciprocity and risk based supervision.

The survey however revealed some contradictions relating to transparency of the supervisory process. While it was established that transparency according to literature and the WTO/GATS model is not applied in regulatory process of NAICOM, responses in the survey did not entirely support that fact but rather contradictory responses were obtained. In response to transparency question under the supervisory process in the IAIS section of the questionnaire, majority of the respondent were of the opinion that the supervisory process lacked transparency when focussing on its dealings with the regulated. However, on regulatory principles, majority of respondents were of the opinion that transparency was applied at least fairly thereby contradicting the earlier responses. As noted earlier, the regulated would rather have lower standards of transparency towards to the public than when dealing with them.

The analysis also revealed some facts about NAICOM that has implications for the liberalisation of the NII. First, that the Commission does administer the NAICOM Act and most of its activities are in line with the IAIS principles except for derivatives and group based supervision which is not relevant to the structure of the NII. The chapter also revealed that NAICOM has been dynamic in its supervisory role making sure that the industry adapts to global standards in insurance regulation, (IAIS,) in financial reporting (IFRS) and in measuring financial strength of insurance companies, International Actuarial Standards Association (IASA). These measures are significant boosters to the liberalisation process. If the NII operates at global standards, then it could compete globally and this would support liberalisation.

Nevertheless, there are some challenges which transparency and accountability. There is no regulatory policy and therefore non-availability of official reports which will inform the public about the activities of the Commission and firms within the market. This thesis continues to reiterate that transparency is crucial to the success of liberalisation, promotion of a healthy and sound NII and invariably the growth and development of the Nigerian economy.

This chapter has concluded all the analysis both doctrinal and survey research response. The next chapter which is the final chapter would detail all the findings from chapter one to six draw conclusions based on the entire research and make recommendations for further research.

## **CHAPTER EIGHT**

### **FINDINGS AND CONCLUSIONS**

#### **8. INTRODUCTION**

This chapter summarises the findings of this research, conclusions and makes recommendations for the liberalisation of the NII and possibly other developing countries in the world. The findings address the research questions set in the introductory chapter while the conclusion and recommendations are based entirely on the findings.

##### **8.1. FINDINGS**

This research is premised on the fact that insurance services provides socio-economic benefits and that reforms and well sequenced liberalisation of the NII in line with the GATS model will enhance the potential for economic growth in the sector.

The first chapter explores the economic outlook and the developmental problems of the country arguing that Nigeria was a flourishing produce exporting economy with growing industrial base until the oil boom period of 1970s. It demonstrates that over reliance on oil caused the neglect and halting of the growth prospects of the other sectors within the economy. It further uncovered the damaging effect of the indigenisation policy of 1972 especially the elimination of foreign participants in many sectors of the Nigerian economy. This policy amplified the growing developmental challenges. The chapter also noted that since Nigeria's return to

democracy in 1999, reform programmes embarked on to attract foreign investors have yielded only moderate results. Also several structural challenges were identified. The analysis further exposed the problems of Nigeria's participation in regional and bilateral trade relations particularly the lack of deep integration and trust amongst African countries. It also revealed the challenges of using non-economic criteria as the basis of commitments in bilateral agreements.

This research effectively related the problems with the NII sector and the inadequacies in the general framework for trade regulation and participation. The chapter argued that greater reforms and liberalisation would be required to promote market efficiency and competition which will facilitate the NII's delivery of growth function to the economy. The chapter successfully argued that a well-structured and liberalised NII would increase the prospects for growth in the economy. It also presented a compelling case for pursuing greater unilateral liberalisation in preparation for more locked in commitments within GATS to support reform programmes. This would ensure efficiency in the domestic market and fuller gains from multilateral commitments subsequently.

Chapter two reviewed the literature on the nature and role of insurance services in the economy together with the regulatory requirement for a successful liberalisation examining its benefits and challenges. The analysis revealed the traditional functions and growth potentials of insurance services in the economy. It presents the regulatory challenges of insurance services and emphasises on the need for appropriate regulations which adopt effective regulatory principles to ensure effective liberalisation of the insurance sector. Through in-depth analysis of the nature of

insurance services and well-balanced arguments on its benefits and challenges, chapter 2 cemented the case for liberalising insurance services particularly in Nigeria

Chapter three mapped out the theoretical and legal framework for liberalisation. It analysed the concept of liberalisation and the tools for achieving effective liberalisation. The discourse revealed the importance of regulations for trade liberalisation generally and specifically for insurance services liberalisation. The chapter launches an effective review of the WTO/GATS framework with in-depth and critical analyses of the GATS general framework for liberalisation. The chapter effectively reiterates the importance and viability of using the GATS model as a liberalisation framework for the NII. The chapter successfully argues that this model promotes flexibility and progressive liberalisation hence its attractiveness as a liberalisation model for developing countries. It brings out the unique structure of the GATS and its liberalisation framework particularly the distinctions between specific and general commitments and the concept of the 'bottom up approach', domestic regulation requirements (such as transparency and adoption of international standards); and discusses the issues particularly of interest to developing countries such as economic integration, technical cooperation, and increasing participation of developing countries.

The chapter concludes by highlighting the fact that the GATS principles and model presents regulatory models on which reforms can be benchmarked.

Chapter four presented the GATS framework of insurance liberalisation with sound legal analyses of the framework of the main agreement specifically guiding

negotiations on insurance in the WTO i.e. The Annex on Financial Services. The contributions of other models such as the Understanding on Financial Commitments and the Insurance Model and Best Practices to the liberalisation framework for insurance under the GATS were also considered. The standards for insurance supervision provided by the International Association of Insurance Supervisors (IAIS), a recognised standard for determining violation of obligations under the GATS Agreement was also reviewed. Pertinent provisions for insurance service liberalisation and regulation including the prudential carve out were effectively analysed and their implication for liberalisation of insurance made bare.

This chapter also considered market access and current negotiations on insurance in the GATS revealing the effect of regulatory regimes of members on liberalisation of insurance in the GATS. The thesis argues that though there is a proliferation of bilateral agreements in insurance, these cannot afford the credibility, transparency and wider framework for trade which the WTO/GATS offer. The detailed evaluation of the GATS model for insurance liberalisation in this chapter, coupled with the other arguments that were developed in other parts of this thesis enabled a major accomplishment of this research; construction of the parameters for the liberalisation of insurance services; as relevant for testing the nature and extent of liberalisation of insurance services sector in developing countries, particularly, in Nigeria.

The parameters include the legislative parameters and the Institutional parameters. The former concerns the adoption of risk based regimes, principles based regulations and the removal of restrictions on market participation. The institutional parameters entail having supervisory objectives, a supervisory authority with adequate powers

and resources (both capital and human) effective independence and accountability and finally supervisory process that is transparent, cooperative with other regulators and employs effective surveillance mechanisms. These parameters formed the model of reforms presented for benchmarking in chapter five and six.

The fifth chapter benchmarked the legislative model of reforms against the legal framework of the NII. It details some startling revelations about the state of the legislative regime that pose challenges for liberalisation of the NII by revealing measures that violated the GATS model, those not violating but not liberal and those supporting liberalisation. Laws violating the GATS were mainly on market access in commercial presence mode such as prescription of the legal nature of branches and in the cross border mode, the guidelines from NAICOM requiring authorisation for reinsurance. Some of the laws which were not in violation of the GATS but would require reforms for greater liberalisation include the tedious process of incorporation, the 5% compulsory session to Africa Re and the unfair interference in the internal administration of foreign firms in visa processing for foreign staff. However, some laws were found to support liberalisation and this include the prompt processing of licensing with NAICOM and the operation of the NIPC's activities in the One Stop Service that fast-tracks incorporation and registration process for foreign firms. It also includes the provision of guarantees against expropriation both by the NIPC and the Foreign Exchange Act. Other favourable provisions of the law include the availability of remedial procedures in the licensing process and application of principles based measures in the corporate governance codes and the Know Your Customer code.

The chapter generally revealed that most of the legislations were obsolete, prescriptive and protectionist in nature. They also favoured the commercial presence mode of trade while being very restrictive on the cross border mode and the temporary entry of natural person mode of trade in services. However, there is no legal provision for the consumption abroad mode of supply.

The chapter concludes with the argument for more reforms in legislation affecting the NII to enable greater liberalisation and competition. This would involve streamlining the procedure for participation of foreign suppliers, adoption of more principle based and risk based regulations as an effective platform for a growth facilitating liberalisation of the NII.

Chapter six continues the legal analysis by focussing on the institutional framework for the regulation and supervision of NII. This involves a critical analysis of the NAICOM Act of 1997 which established the NAICOM benchmarking it against the institutional model of reforms for insurance services liberalisation constructed in chapter three. The analysis revealed that the Act provided a clear supervisory objective but with no emphasis on consumer protection which is a major objective for insurance regulation globally. It further uncovered gross inadequacies in the provisions of the NAICOM Act particularly in terms of the powers, resources, independence and accountability of the Commission. Also there are no provisions for regulatory cooperation between the NAICOM and other relevant regulators and transparency while the surveillance structure was found to be inadequate. The chapter successfully canvassed the need for institutional reforms which will address the institutional challenges identified for supervisory effectiveness to attune it with the

institutional parameters of liberalisation derived from the GATS Model. The NII should give consideration to the adoption of a Bi-Polar system of financial regulation where financial services are supervised by two bodies with the central bank supervising deposit taking companies while a new agency would be created to supervise the non-deposit taking firms like insurers and capital market firms. This would help in pooling resources and alleviating the challenges of resource and staffing inadequacies currently in NAICOM. The new agency for the non-deposit-taking financial sector would be independent, well-staffed and employ PBR and risk based prudential regimes.

Chapter seven presented the data from the survey research conducted on the NII. The responses reveal the demographic characteristics of the research population and provide data that compliments the findings from the doctrinal analysis particularly in chapters 2 to 6 of the thesis. The findings of the survey confirm the legislative and institutional inadequacies of the NII with regards to liberalisation. However, there was some disagreement about the transparency levels of the NII which suggested respondents' double standards on transparency.

This work has reiterated through each chapter the main theme of this thesis namely: that liberalisation of the Nigerian insurance sector using the GATS regulatory model is vital for efficiency, growth and development of the sector and Nigerian economy as a whole. Currently, structural challenges inhibit the sector from effectively performing its growth functions in the economy. The NII invariably require reforms both in the institutional and legal framework of the sector. Areas suggested include: transparency, proportionality, consumer protection, risk based prudential regimes and

the easing of restrictions on market participation in insurance services especially in the cross border, and temporary entry of natural persons mode of supply. This thesis argues that these reforms would prepare the domestic market for more lock-in commitments in the GATS which will ensure credibility of domestic reforms and subsequently produce gains from trade from reciprocated market access.

## **8.2 FINAL CONCLUSIONS**

- a) This thesis concludes that the reforms and liberalisation of insurance services can be employed as a vehicle of economic growth in Nigeria using the GATS model.
- b) To achieve the growth function of the NII, this thesis submits that there is the need for adoption of a liberalisation and competition policy by government with effectively sequenced legal and institutional reforms. This is because the legal and structural framework of the NII is currently inefficient, ineffective and anticompetitive therefore the sector cannot contribute effectively to the growth of the Nigerian economy.
- c) This thesis submits that there is also need for sweeping reforms in the financial sector to streamline the legal framework for foreign participation in the financial sector generally. Foreign participation is required for the NII to experience increase in investment capital, capacity, innovative products, and transference of superior skills which would translate into greater profit and increasing GDP.
- d) It further submits that supervisory arrangement in NAICOM needs to change for a robust independent agency with adequate independence and resources. This can be achieved by adopting the bipolar supervision which

separates supervision of deposit taking institutions in the financial sector from non-deposit taking ones as earlier noted in chapter six.

- e) Reforms should include policies geared towards increasing the level of insurance awareness to facilitate higher levels of insurance penetration and density in Nigeria. Concessions should be given to firms which promote PIL. This should be preceded by the introduction of greater transparency, openness, consumer protection and prudential management of the firms in the NII.
- f) Finally, the findings of this study would be of importance not only to Nigeria therefore it is recommended for other developing countries desirous of economic development.

### **8.3 SUGGESTIONS FOR FURTHER RESEARCH**

It is suggested that future research in this area could consider looking into the workability of the unification of supervisory agency for non-bank financial institutions as a model for African countries. This would be geared towards solving the problem of regulatory capacity and cooperation currently plaguing the region.

**APPENDIX**

**SURVEY QUESTIONNAIRE**

**PHD RESEARCH ON INSURANCE REGULATION IN  
NIGERIA BY *MRS YESIDE ABIODUN OYETAYO***

**PARTICIPANT INFORMED CONSENT FORM**

I Respondent No. ----- agree to participate in the above research as a respondent having been assured of anonymity and the confidentiality of my responses. I agree that my responses would be used solely for research with utmost academic independence.

SIGN .....

DATE .....

## STRUCTURED INTERVIEW FOR RESPONDENTS

### Part A

#### 1. Conditions for effective insurance supervision

##### 1. Insurance supervision-

- i. Does NAICOM rely upon
- ii. a policy,
- iii. Institutional and legal framework?
- iv. Does the insurance industry exist within a well-developed financial market and infrastructure?

#### 2. The Supervisory System

##### A. Supervisory Objectives

- i. Are the supervisory objectives clearly defined? What are the supervisory objectives of

##### B. Supervisory Authority –

- i. Does NAICOM have adequate
  - a. powers,
  - b. legal protection,
- ii. financial resources?
- iii. Is NAICOM operationally independent and accountable in exercising its functions and exercising these functions and powers?
- iv. Is NAICOM able to 'hire, trains and maintains sufficient staff with professional standards?

##### C. Supervisory Process –

- i. Does NAICOM conduct its functions in
  - a. a transparent or
  - b. accountable manner?

##### D. Supervisory Cooperation and Sharing – Does NAICOM cooperate and share information with other relevant supervisory bodies subject to confidentiality

requirement?

### 3. The Supervised Entity

- a) **Licensing** – is licensing of insurers done through a
  - i. clear,
  - ii. objective criteria, qualification and technical requirements.
  - iii. public process?
- b) **Suitability of Persons**- Are owners, board members and management staff including actuaries and auditors of insurance companies persons fit and proper possessing not only professional qualification and also persons of integrity, competence and experience?
- c) **Changes in Control and Portfolio Transfers**- Are proposals by an individual whether directly or indirectly to acquire ownership or interest in an insurer presented to the regulatory authority either for its approval or reject? Also, are mergers and portfolio transfers must be approved by this body?
- d) **Corporate Governance**- Are the rights of all parties of interest recognized and protected? Is compliance with this required of the NAICOM through such measures as corporate discipline, transparency, accountability, fairness and social responsibility to mention a few? Is the board being the focal point of governance system?
- e) **Internal Control** – Are internal controls system of insurance companies commensurate with the scale of business and enable both board and management to monitor and control the operations of the business

### 4. On-going Supervision

- A. **Market Analysis** – Does NAICOM monitor and analyse factors that affect the market, draw conclusions and take appropriate action?
- B. **Reporting to Supervisors and Off-site Monitoring**- Does NAICOM receive enough information to be able to do off-site monitoring and evaluation of the market and individual insurers?
- C. **On-Site Inspection** – Does NAICOM do on-site inspection to ascertain conformity with legislative and supervisory requirements?
- D. **Preventive and Corrective Measures** – Does NAICOM take preventive measures to achieve the supervisory objectives?

- E. Enforcement of Sanctions** – Does NAICOM where needed, enforce corrective action and impose publicly disclosed sanctions that are clear and objective?
- F. Winding –up and exit from the market** – Is there are a range of options for orderly exit from the market through legislative and supervisory means? Are there well defined solvency provisions and procedures for dealing with it which gives priority the protection of policyholders?
- G. Group-wide Supervision** – Does NAICOM do group-wide supervision both on solo basis and group-wide basis? Is Group wide supervision done on insurance companies belonging to a group to ascertain the extent to which the activity of the group may affect the insurance companies’ financial stability?

## 5. Prudential Requirements-

- a. Risk Assessment and Management** – Does NAICOM do effective risk identification, assessment and management?
- b. Insurance Activity** – Does NAICOM ensure that insurers do risk evaluation and management through reinsurance and also have tools to ensure adequacy of levels of premium?
- c. Liabilities** – Does NAICOM require compliance of insurers to standards of technical provisions and other liabilities and does it have the requisite authority to determine the adequacy of this provisions and possibly increase these provisions?
- d. Investments** – Does NAICOM ensure compliance with investment standards such as investment policy, asset mix, diversification and asset-liability matching?
- e. Derivatives and Similar Commitments** –Does NAICOM ensure compliance with standards on the use of derivatives and similar commitments and especially on restrictions and disclosure requirements as well as internal controls and monitoring?
- f. Capital Adequacy and Solvency** – Does NAICOM ensure compliance with solvency regime including capital adequacy requirements and suitable forms of capital that would enable insurer absorbs significant losses?

## 6. Market and Consumers

- a. Intermediaries** – Does NAICOM set requirements for the conduct of business by intermediaries either directly or through the supervision of insurers?

- b. **Consumer Protection** – Does NAICOM set minimum requirements for insurers and intermediaries in dealing with consumers including foreign insurers selling products on cross-border basis? This includes timely, complete and relevant information before a contract of insurance is entered into.
- c. **Information, Disclosure and Transparency Towards The Market** – Does NAICOM ensure that insurers disclose timely and relevant information that gives a clear view to stakeholders about the financial status of their business and an understanding of the risks which they are exposed to?
- b. **Fraud** –Does NAICOM ensure insurers take measures to prevent, detect and remedy insurance fraud?

**7. Anti-money laundering, combating the financing of terrorism (AML/CFT)**

Does NAICOM take measures to deter, detect and report money laundering and financing of terrorism?

## **Part B**

### **REGULATORY PRINCIPLES**

#### **Which regulatory principles do Nigeria apply**

- a. Transparency-
- b. Local protectionism or Free Trade and Competition-
- c. Reciprocity-
- d. Proportionality- i.e. laws are proportional to the objectives for which they were made.
- e. Risk Based Regulation-

## **Part C**

### **COMPLIANCE WITH INSURANCE MODEL SCHEDULE**

- 1. **Market Access on Cross Border Supply of reinsurance and transport insurance including marine and aviation :**
  - a. Is there market access without any form of restrictions irrespective of whether they are domestic or foreign insurance companies?
  - b. Are there mandatory cessions?

- c. Are there restrictions on cessions to foreign or of privilege of first refusal for domestic reinsurance suppliers, or discriminatory requirements on foreign reinsurance suppliers on localization of assets and collateralization been done?

**2. Market Access for Commercial Presence mode:**

**a. Form of establishment,**

- i. Can a foreign supplier set up a subsidiary with 100% ownership or partly owned
- ii. Can foreign supplier provide the insurance services in Nigerian market using its home company name provided it does not infringe on existing trademark.
- iii. Can foreign suppliers denied access on the basis of its legal nature at home.

**b. Equity Shareholding**

- i. Where commercial presence is to be by joint venture, is the percentage of equity shareholding of the foreign supplier determined solely by the parties themselves.
- ii. Are foreign equity share restrictions eliminated if necessary over a transition period not to exceed two years during which the foreign partner should be allowed at least 51% of the company?

**c. Compulsory Insurances:**

- d. Are there restrictions to foreign suppliers on compulsory Insurance?

**e. Monopolies**

- i. Are they allowed.

**f. Pension Fund Management**

- i. Does Nigeria currently allow private participation in pension systems
- ii. Are foreign suppliers with commercial presence allowed to participate on non-discriminatory basis.

**3. Market Access for Temporary Entry of Natural Persons:**

- i. Is there Market Access for Temporary Entry of Natural Persons:
- ii. Requirements on nationality avoided.
- iii. Are foreign suppliers maintaining a commercial presence at liberty to choose competent representatives who will physically reside?
- iv. Is temporary visa for professionals employed by foreign suppliers timely.
- v. National Treatment -Are foreign suppliers also able to compete for insurances of state owned enterprises or enterprises?

- vi. Are these foreign suppliers treated 'less favourably than domestic suppliers with respect to capital, solvency, reserve tax and other financial requirements'
- vii. if prudential regulations are to be used does NAICOM explain the basis?

## **Best Practices under GATS**

### **Please state the extent to which NAICOM abides with any of the following requirements**

This is to be assumed under Additional Commitments (Article XVIII) of other than those under market access and national treatment. It proposes the following:

- a. With regards to transparency requirement:
  - 1. New and existing regulation including revisions to existing law is made publicly available.
  - 2. New or revised laws are submitted for public scrutiny and comment before it is enacted.
  - 3. An insurance supplier applying for license should get a written statement setting out information.
  - 4. There are established procedures for ascertaining credit worthiness of insurance companies by customers.
  - 5. Subject to GATS provision for exemptions to protect privacy of individuals members shall ensure availability of '*financial services information from domestic or foreign sources to registered insurance suppliers*' (para 7)
  - 6. Non-discriminatory rules and procedures govern identification and handling of financially troubled institutions.
  - 7. Taxation measures that affect insurance do not enter into force until it has been notified WTO through a semi-annual notification process.
- b. **Solvency and Prudential Focus**
  - Filing and approval not required for new products or rates except for compulsory insurances.

- No restrictions on payment of dividends by foreign insurance companies provided solvency requirements are met.
- Encourage the adoption of best practices as

c. Insurance Monopolies

1. Prohibited from operating outside their area of monopoly.
2. Insurance monopolies maintain separate accounts for monopoly and non-monopoly activities.
3. Independent Regulatory Authority

**PERSONAL DETAILS**

**PLEASE CIRCLE THE APPROPRIATE ANSWER OR SPECIFY WHERE  
REQUIRED**

**1.GENDER: a. MALE                      b. FEMALE**

**2. AGE:                      a. 25- 30                      b. 40-50                      c. 50 -60**

**3. GROUP: a. BROKING  
                    b. INSURANCE COMPANY  
                    c. NAICOM OFFICIAL  
                    d. POLICYHOLDER**

**4. QUALIFICATION:            a. LOWER DIPLOMA  
    b. HIGHER DIPLOMA  
    c. BACHELORS DEGREE (Specify) .....  
    d. MASTERS DEGREE (Specify) .....**

**4. POSITION (Specify) .....**

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