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Voluntary Public

Date: 8/22/2011

GAIN Report Number: RS1138

Russian Federation

Post: Moscow

Federal Law on State Support of Agricultural Insurance

Report Categories:

Agricultural Situation

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Report Highlights:

On July 25, 2011, Russian President Dmitry Medvedev signed the Federal Law on the State Support of Agricultural Insurance. The law enlarges the list of insured risks and products, and increases guarantees of compensation payments. However, this framework law neither determines budget funds, nor the actual mechanism of this budget support.

General Information:

State Supported Agricultural Insurance in 2007-2010

In 2006 the Federal Law On Developing Agriculture (No. 264-FZ of December 29, 2006) extended federal support to crop insurance. However, the scheme of government support was burdensome to farmers: they were receiving 50 percent compensations of the premium only after they paid the whole premium themselves (the time lag might be several months). In many cases the insurers refused paying compensations blaming the losses on the farmer's poor agronomic practices. Because of its expensiveness, unfair practices of many insurance companies, complicated insurance procedures, and unpredictable government policy of losses compensations, the farmers largely ignored the state-supported insurance. Besides, the federal funds for support of crop insurance were decreasing. In 2008 the federal budget allocated 3.4 billion rubles (\$113 million) for crop insurance support, but in the budget of 2010 these allocations decreased to 2 billion rubles (\$66.7 million). Only drought 2010 forced the government to increase budget funds for compensation of crop insurance premiums to 3.5 billion rubles (\$117 million) in October 2010.

Table 1. Russia: State Supported Crop Insurance, 2007 -2010

	2007	2008	2009	2010 ⁱ
Number of farms (all types) that concluded crop insurance agreements	10,143	8,256	5,742	3,919
Including				
• agricultural organizations	6,947	4,807	3,637	2,365
• private farms	3,196	3,449	2,105	1,554
Share of insured crop lands in arable land, %	28.3	25.0	18.2	13.0
Number of insurance companies with state-supported insurance	69	61	64	49
Insurance volume, million rubles	113,918.5	123,258.4	119,126.8	87,982.8
Insurance volume, million \$US ⁱⁱ	3,797.3	4,108.6	3,970.9	2,932.8
Paid insurance premiums, million rubles	7,727.6	8,794.7	9,184.3	8,805.8
Paid insurance premiums, million \$US ⁱⁱ	257.6	293.2	306.1	293.5
Federal subsidies, million rubles	3,065.2	3,400.0	2,494.9	3,503.6
Subsidies from provinces, million rubles	772.8	878.5	1,101.6	792.7
Federal subsidies, million \$US ⁱⁱ	102.2	113.3	83.2	116.8
Subsidies from provinces, million \$US ⁱⁱ	25.8	29.3	36.7	26.4
Share of actual state compensations in insurance premiums, %	49.6	50.3	39.1	49.0
Farms that received state compensations	5,155	4,870	1,947	2,130
Insurance compensations received by farmers, million rubles	4,145.8	5,325.7	4,523.1	6,372.4
Insurance compensations received by farmers, million \$US ⁱⁱ	138.2	177.5	150.8	212.4

- i. in CY 2010 the federal funds for the state support insurance were increased from the planned 2 billion rubles to 3.5 billion rubles in October 2010 in order to help the compensation payments to drought-affected farmers.

- ii. In 2007 -2010 the exchange rates changes often, and for comparisons FAS Moscow sets the exchange rate at 30 rubles per U.S.\$1

Source: Ministry of Agriculture of the Russian Federation. National Report on the Implementation of the State Program on Development of Agriculture 2008-2012 in 2010.

The droughts in 2009 and in 2010 revealed that agricultural insurance works poorly in Russia. On August 17, 2010 the confirmed damage of agricultural crops in 23 provinces was 30 billion rubles (\$1 billion)^[i]. Industry analysts estimated that only 10 to 20 percent of crops were insured by farmers in 2009-2010. In some drought-affected provinces the share of insured croplands was less than 10 percent. Most of insured cropland was in the big agro-holding companies for which insurance is a requirement for receiving commercial loans, whether the insurance is on terms of government support or without. Rosgosstrakh, Russia's major insurance company, reported that only very big enterprises can afford insurance without government support.

Federal Law No 260 FZ On the State of Agricultural Insurance

After the disastrous drought in 2010, farmers and authorities of all levels acknowledged the drastic need for a new system of support of insurance of agricultural production against nature-caused risks. On July 25, 2011, Russian President Dmitry Medvedev signed the Federal Law (No. 260-FZ) On the State Support of Agricultural Insurance and On Amendments to the Federal Law On Developing Agriculture. The Law was published in Rossiyskaya Gazeta: <http://www.rg.ru/2011/07/27/selhoz-dok.html>.

This Federal Law regulates the terms and conditions of state support in insurance of agricultural production against natural disasters. The state-supported insurance will cover risks of losses of agricultural crops, orchards, and livestock. The term "losses" means the decrease of the actual crop by up to 30 percent from the planned level and up to 40 percent losses of the orchard planted area. The law will reduce farmers' payments to 50 percent of insurance premium, while the other 50 percent will be paid to the insurance company by the government. Beginning from 2013, the state-supported insurance will be expanded to livestock production.

The drafters of the law report that the new law may allow farmers to increase insurance coverage to 70 percent of Russia's crop land. The law stipulates that the insurance companies will unite in order to guarantee that compensations are paid even in cases of bankruptcies of individual insurance companies. The union of insurance companies will form a special fund of compensation payments formed at the expense of part of insurance premium on agricultural insurance agreements.

The amount of federal allocations for support of agricultural insurance will be based on the "annual plan of agricultural insurance", which is formed on the basis of proposals of subjects of federation and associations of insurance companies. The drafts of regulations for implementation of this federal law are to be worked out by the government of the Russian Federation.

The new scheme of state-supported agricultural insurance will start working in 2012, but in 2011 the federal budget already increased state funds for support of crop insurance to 5 billion rubles (\$167 million) Thus, even under the former rules, the crop insurance may increase in 2011.

The summary of the Federal Law No. 260-FZ is in the Appendix 1 to this report. The Federal Law

comes to force on January 1, 2012. Provision on the state support of insurance of farm animals comes to force on January 1, 2013, and provision on the compensation payments by associations of insuring companies comes to force on January 1, 2014.

Comments

The new federal law on the state support in agricultural insurance is aimed at direct compensations of farmers' premium payments, and extends state support to insurance of livestock production, thus making a step forward in developing a uniform scheme of state support of agricultural insurance.

However, the law is a framework one, adopted in a hurry, and requires many additional regulatory government documents. The Article 3 stipulates that "the order of state support in the field of agricultural insurance is established by normative legal acts of higher executive authorities". Thus, the final procedures will depend on the competency and good-will of these executive authorities. Commenting on the just signed 260-FZ, Russian President Dmitry Medvedev pointed out at the meeting in Tambov on July 25, 2011 that the document is a framework one and some ideas may need additional real instruments, such as a standard insurance contract, a third-party body for resolution of conflicts between farmers and insurance companies. He also supported the idea to increase the number of instruments for collateral, such as warehouse receipts, and the idea of common work with international insurance companies, after Russian insurance companies reach an agreement between themselves.

There are a few limitations of the Federal Law, which may diminish its effect:

- The law does not determine the level of federal budget financing of the state support. This financing will be subordinated to the annually changing priorities of Russia's federal budget;
- The rules of the law determine that the estimates of losses will be based primarily on physical, not value, parameters of losses. Thus, the estimates will continue to be dependent on the expertise and the goodwill of insurers. The elaborate norms that might be developed by the "executive authorities" for estimation of losses might be difficult to follow if they are not based on price analyses. The physical parameters based approach is outdated. In the developed countries the insurance programs switch to insuring farmers' revenues rather than physical volumes of lost crops. Thus, this federal law will provide only some protection from natural disasters, but will not provide any protection from market vulnerability and price fluctuations, and will not guarantee stability of farmers' business.
- In cases of bankruptcies of individual insurance company, the law envisages that compensation payments will be paid from the fund of compensation payments created by the association of insurers. However, the provision on such compensation payments comes to force only on January 1, 2014, when the association of insurers is created. In the meantime the insured will not have guarantees in case of bankruptcy/preparation to bankruptcy of insurer.
- The 260-FZ does not clarify, whether the presence of the state-supported insurance contract is a mandatory requirement for farmer's participation in all other state-supported programs, or not (Article 11 of the 260-FZ), and does not specify who might make such decision.

^[i] Source: Interview with the First Deputy Prime Minister Viktor Zubkov, Rossiyskaya Gazeta, August 17, 2010

Appendix 1:

Summary of the Federal Law No. 260-FZ

Unofficial, abbreviated translation.

Federal Law No. 260-FZ of July 25, 2011

On the State Support in the Sphere of Agricultural Insurance and on Amendments to the Federal Law on Development of Agriculture

Adopted by the State Duma on July 5, 2011

Approved by the Federation Council on July 13, 2011

Article 1. Subject of the present Federal Law

“This federal law establishes the legal framework of state support in the field of insurance of property interests of agricultural commodities producers related to agricultural production”.

Article 2. Basic terms used in this Federal Law

This article specifies the terms used in the Federal Law, such as, the beneficiary, forced slaughter of farm animals, mortality of farm animals, the association of insurers, agricultural crops, yields (production), the insured, the insurer, etc. The term “loss (destruction) of agricultural crops” during the period of insurance contract means that the actual crop production (yield) decreased by 30 percent or more compared to the planned harvest as a result of the events specified in Article 8. The term “loss (destruction) of planted perennial crops” [orchards] during the period of insurance contract means that orchards lost its vitality on more than forty percent of planted area as a result of the events specified in Article 8. The term “loss (death) of farm animals” during the period of insurance contract means mortality or forced slaughter of farm animals as a result of the events specified in Article 8 of the Federal Law.

Article 3. The order of state support in the field of agricultural insurance

The law stipulates that the concrete acts, regulations and requirements for implementation of the present federal law are to be set by the normative acts of the executive authorities of the Russian Federation or the subjects of the Russian Federation, such as resolutions of the federal government, normative documents of the ministries, etc. The normative documents cover such concrete spheres of state support in the field of agricultural insurance as the procedure of support, procedure and norms of distribution of budget subsidies for this support, methodologies of calculation of cost of insured crops/animals, losses, insurance premiums and loss coverage, terms of transfer of the subsidies to provinces and then to agricultural producers.

Article 4. Requirements for agricultural insurance contract

Government supports agricultural producers on the basis of agricultural insurance contracts that meet the following criteria:

1. The contract is concluded between the insurer and the insured in accordance with the provisions of this federal law, including provisions of Article 6 hereof about the insurance plan for the relevant year.
2. The contract is concluded:
 - a) in respect of agricultural crops, planted orchards on the entire area on which agricultural

producers grow crops, orchards;

b) in respect of all farm animals of a certain type at the agricultural producer;

3. The contract is concluded:
 - a) in respect of crops, except for orchards, not later than fifteen calendar days after the end of the sowing or planting;
 - b) in respect of orchards, before the termination of their vegetation (transition to a state of winter dormancy);
 - c) in respect of farm animals, for a period of not less than one year;
4. The contract of agricultural insurance came to force, and agricultural producers paid fifty percent of the accrued insurance premium;
5. The agricultural insurance contract may not be terminated prior to the date on which it was made, except as provided in Article 958 of the Civil Code of the Russian Federation;
6. The sum insured in the contract is set at not less than eighty percent of the insurable value of crop, orchard, farm animals;
7. participation of the insured in the insurance of agricultural risks referred to in Article 8 of this Federal Law shall not exceed forty percent of the sum insured under a contract of agricultural insurance. This share is taken into account when determining insurance rates. The participation of the insured in the insurance coverage means that the insured covers part of the losses him/herself. These losses are not covered by the insurer;
8. the share of insurance premium used in the calculation of insurance rates for insurance and compensation payments to policyholders and beneficiaries cannot be less than eighty per cent;
9. Estimates of the cost of insured crop, orchards, farm animals and the volumes of losses are based on methods prescribed in Article 3 hereof.

Article 5. Examination of the contract of agricultural insurance

In cases of disagreements between the insured and the insurer, the insurer shall examine the case with the help of independent experts, and based on the rules and procedures approved by the Russian Federation.

Article 6. Agricultural Insurance Plan

The Agricultural Insurance Plan is developed by the authorized body on the basis of proposals of the provincial authorities and the Association of Insurers. The Agricultural insurance plan is approved by the competent authority annually, not later than April 30th of the year preceding the planned year. The approved plan is sent to provinces for publication on the internet sites of provincial authorities not later than August 1 of the year preceding the planned year.

The Agricultural Insurance Plan includes: a list of objects of agricultural insurance by species, groups of crops, types of orchards, breeds, age composition of farm animals; the maximum rates for calculation of subsidies, differentiated by provinces and by objects of agricultural insurance.

Article 7. The objects of agricultural insurance

1. In insurance of agricultural crops and perennial plantings (orchards, plantations) the objects of insurance are property interests of the insured related to the risk of loss of crops (grains, pulses, oilseeds, technical crops, such as corn, sugar beet, etc., fodder crops, melons and water melons, potatoes, vegetables, vineyards, fruits, berries, nut trees, plantation of hops, tea), loss of

perennial plantings, such as vineyards, fruit plantations, nut plantations, plantations of hops, tea.

2. In insurance of farm animal the objects of insurance are property interests of the insured related to the risk of loss of the following types of farm animals:
 - 1) cattle (buffaloes, bulls, oxen, cows, yaks);
 - 2) small ruminants (goats, sheep);
 - 3) pigs;
 - 4) horses, hinnies, mules and donkeys;
 - 5) camels;
 - 6) deer (deer, sika deer, reindeer);
 - 7) rabbits, fur-bearing animals;
 - 8) bird species in egg production and poultry meat breeds (geese, turkeys, chickens, quail, ducks, guinea fowl), chicken-broilers;
 - 9) bee families.

Article 8. Agricultural risk insurance which is carried out at government support

1. Concerning crop losses (destruction) and losses of perennial plantings (orchards, plantations) the state supports insurance of losses resulted from the impact of the following events:
 - 1) exposure to dangerous natural phenomena (atmospheric, soil drought, dry hot winds, ground frost, frost-killing, damping off, hail, dust storm, sleet, floods, spring flood, strong winds, hurricane, earthquake, landslide, mudflow, natural fire);
 - 2) penetration and (or) the spread of harmful organisms, if such events are of epiphytoty character;
 - 3) the interruption of electric and thermal energy, water supply as a result of natural disasters for insurance of crops grown in greenhouses or on reclaimed land.
2. Concerning farm animal losses the state supports insurance of losses (death) of farm animals resulted from the impact of the following events:
 - 1) contagious animal diseases included in the list approved by the authorized body, mass poisoning;
 - 2) natural disasters (lightning, earthquake, dust storm, hurricane, severe storm, blizzard, snow storm, flood, landslide, avalanche, mudflow, landslide);
 - 3) the interruption of electricity, heat, water from natural disasters if the conditions of farm animals include the mandatory use of electricity, heat, water;
 - 4) fire.

Article 9. Legal status of association of insurers

The article describes the principles of creation and the targets of the Association of insurers as a nonprofit organization. It will be a voluntary, non-profit association that will develop the uniform rules for agricultural insurers, and will supervise the implementation of these rules, forms the fund for compensation payments and provides compensation payments, participates in preparation of the draft plan of agricultural insurance and methodological documents for estimates of insured products, accumulate and store statistical data, and perform other functions stipulated by constituent documents of the association of insurers.

Article 10. Compensation payments under the agricultural insurance

The article stipulates that in cases when the insurer cannot pay the insurance compensation, the compensation is paid by the association of insurers from the fund of compensation payments. The compensation fund is formed by insurers' contributions of part of insurance premiums received under

contracts of agricultural insurance. The size of such payments is established by the association of insurers for each year, but cannot be less than five percent of the premiums received under contracts of agricultural insurance.

Article 11. Amendments to the Federal Law "On the Development of Agriculture"

The article amends the Federal Law of 29 December 2006 N 264-FZ "On the Development of Agriculture" (Collection of Legislation of the Russian Federation, 2007, N 1, Art. 27, 2008, N 24, Art. 2796) by adding the following sentence to Part 3, Article 7: "The allocation of the federal budget subsidies to provincial budgets for support of production of agricultural products may require that agricultural producers (except household producers, and agricultural consumer cooperatives) have concluded the state-supported agricultural insurance contracts"; and by stipulating that the legal framework of the state support in the field of agricultural insurance is set by the new federal law on the state support of agricultural insurance.

Article 12. Entry into force of this Federal Law

1. This Federal Law shall enter into force on January 1, 2012.
2. The provisions of this federal law relating to the state support for agricultural insurance contracts in respect of farm animals, enters into force on January 1, 2013.
3. The provisions of this Federal Law on the compensation payments by the association of insurers come to force on January 1, 2014.
4. Agricultural insurance plan for 2012 shall be approved not later than February 1, 2012.