THE IMPLEMENTATION OF MICRO-INSURANCE; THE ROLE AND PERSPECTIVE OF THE SUPERVISORY AUTHORITY

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Introduction

- Micro-insurance is defined as *“insurance that is accessed by low-income population, provided by a variety of different entities, but run in accordance with generally accepted insurance practices”*

IAIS Issue Paper on micro-insurance

Key features of micro-insurance

Traditional insurance

- Premiums are regular and paid by cheque or direct bank debit
- Sold by licensed agents to wealthy individuals and businesses
- Large sums insured

Micro-insurance

- Premiums are frequent but irregular. Usually paid in cash or associated with other transactions
- Sold by unlicensed and non-traditional intermediaries to low-income persons
- Very small sums insured

Key features of micro-insurance 2

<u>Traditional insurance</u>

- Detailed underwriting requirements
- Complex policy document with many exclusions
- Pricing based on age and specific risk conditions

<u>Micro-insurance</u>

- Usually relies on confirmations of trusted third parties
- Very simple policy documents with few or no exclusions
- Community or group pricing

The need for micro-insurance in West Africa

- Low insurance penetration
- Majority of the population operate in the informal sector and thus do not have access to mainstream financial services
- Lack of access to financial services cause and worsen poverty
- There is therefore the need for active involvement of all stakeholders to develop micro-insurance in West Africa

Should micro-insurance be regulated?

- It is argued that regulation of micro-insurance stifles innovation and increases operational costs.

- This argument however cannot be wholly accepted without due regard to the objectives of insurance regulation.

Objectives of insurance regulation

- Protection of policyholders from abuse, mis-selling and improper claims handling
- Ensuring financial stability in order to maintain and increase the confidence of the insuring public in the financial system
- Improving efficiency and accessibility of insurance market to those who currently do not have access.

Implications of non-regulation

- No protection for the poor and vulnerable policyholders.
- Long-term viability of the schemes cannot be ensured.
- It will be difficult for micro-insurance schemes to obtain reinsurance support. It will therefore be susceptible to collapse under the slightest stress.
- The conclusion therefore is that micro-insurance should be regulated, but probably with a different or an appropriate approach

How should micro-insurance be regulated?

- There are two main approaches;

  - the activity based (functional) approach and

  - the specialization (institutional) approach.

Functional approach

- The functional approach is where Micro-insurance is offered as a line of business (product line) by any insurance company that wishes to do so.

- Such insurance companies would, apart from their conventional regulatory requirements, have to comply with reporting, underwriting, transparency, dispute resolution, delivery channel and claims handling requirements with respect to their micro-insurance business.

- This approach allows all insurance companies to be treated equitably. There is a level playing field. Regulatory arbitrage is therefore minimized or completely eliminated.

Institutional Approach

- With the Institutional approach, Micro insurance is carried out by special purpose institutions usually called Micro-insurance Institutions. Such institutions are usually given lower entry requirements with regard to capital and key management.

- They are also given lower regulatory requirements (as compared to traditional insurers) with regard to reporting, actuarial reviews and intermediaries. Tax incentives are also used sometimes to attract investors.

- Although the Institutional approach has the advantage of making it easier to set up specialized micro-insurance institutions which helps to increase access to the poor, by its very nature, it breeds regulatory arbitrage.

Other Regulatory Challenges

- Distributions system of traditional insures are not designed to serve the low-income market.
- Regulatory requirements may inhibit the use of innovative distribution channels.
- Products are not designed to meet the specific characteristics of the low-income market.
- Micro-insurance target markets often lack insurance information and understanding.
- Protection from abuse is therefore difficult.
- Lack of appropriate channels of complaints and dispute resolution.
- The need for composite services as against the current trend towards separation.

The experiences of Supervisory Authorities of some emerging market economies

- India
- South Africa
- Philippines

India

- The IRDA has introduced a quota system to compel the insurance companies to serve the poor.
- Micro-insurance regulations have been issued to set appropriate rules for micro-insurance.
- The regulations allow NGOs, MFI, and other community based organisations to be used as micro-insurance intermediaries.
- The regulations also allow the bundling of life and non-life elements in one single product provided there is clear separation of premiums and risk at the insurers end.

South Africa

- South Africa is considering a second tier funeral insurance licence with reduced entry and compliance requirements.

- A public-private dialogue has also led to the adoption of a Financial Sector Charter whereby all financial service providers have agreed to voluntarily serve the low-income market. As a result, the South African insurance industry has experienced a huge wave of innovation as insurers experiment with new delivery channels to reach the poor.

- Under the Charter, the Financial Services Board (FSB) is responsible for facilitating, funding, monitoring and coordinating better consumer education.

Philippines

- The Insurance Commissioner in the Philippines has created a second tier system which allows Mutual Benefit Associations (MBAs), once they become significant enough to be “noticed” in terms of volumes and membership numbers, to be registered and licensed by the Commissioner.

- MBAs are subject to supervision and need to have access to an actuary. The Insurance Commissioner has set up a special MBA unit to supervise them. Agents of MBAs do not require licences.

- On major feature of the MBAs is the high income tax differences between commercial insurance companies and these second tier institutions which are supposed to deter conversion into a first tier insurance company.

What should West African Supervisory Authorities do?

- Developing laws and regulations, as well as supervisory practices that are suitable to the peculiar characteristics of micro-insurance.
- Requiring disclosure regarding involvement in micro-insurance from regulated risk carriers.
- Researching into and information on market needs, which may motivate insurers to reach out to the low-income market.
- Allowing micro-insurance providers to use new and innovative distribution channels that are familiar with, and have the trust of low-income households.
- Creating grievance channels and resolution systems appropriate for low income policyholders.

What should West African Supervisory Authorities do? (cont'd)

- Embarking on effective educational campaigns to increase understanding of insurance and promoting policyholder awareness of their rights and benefits.
- Ensuring that products and procedures are tailored to suit the needs of the low-income households. Appropriate micro-insurance policy wording requirements should be developed to ensure that insurance policies for the poor are concise, brief and written in very simple language so that the terms and conditions are easily understood.
- Facilitating dialogue with policymakers and relevant stakeholders to develop effective private-led market oriented micro-insurance.

Thank you