Report of the 16th A2ii – IAIS Consultation Call

Regulatory Definition of Microinsurance II

19 May 2016

The A2ii consultation calls are organised in partnership with the IAIS to provide supervisors a platform to exchange experiences and lessons learnt in expanding access to insurance.

The 16th Consultation Call, held on 19 May 2016, focused on regulatory definitions of microinsurance and served as a follow-up to the A2ii's first ever Consultation Call on the same topic that took place in March 2014. Four calls were held: two in English, one in French and one in Spanish.

Technical experts Martina Wiedmaier-Pfister (independent consultant and inclusive insurance expert) and Andrea Camargo (Director of Regulation and Consumer Protection of the Microinsurance Catastrophe Risk Organisation, MiCRO) presented on the objectives, key elements and challenges of establishing a regulatory definition of microinsurance. On the second English call Michael Kofi Andoh (National Insurance Commission Ghana) shared Ghana's experience of developing a microinsurance definition, and on the Spanish call Carla Chiappe (Superintendencia de Banca, Seguros y AFP del Peru) shared Peru's experience with updating and adjusting their regulatory definition.

Introduction

Establishing a microinsurance definition is generally the starting point for any microinsurance regulation. A definition of microinsurance ensures that regulation can be tailored to the risk profile of insurers writing inclusive insurance business as well as the risk profile of the typically more vulnerable inclusive insurance consumer. Once an appropriate regulatory definition for microinsurance is in place, it helps support the development of inclusive insurance markets in a jurisdiction.

Objective and Key Elements of a Microinsurance Definition

Prior to establishing a microinsurance definition it is necessary to consider first *what* is to be defined as well as *why* a regulatory definition is important to begin with.

→ What is regarded as 'microinsurance' can vary across jurisdictions. Generally, it is insurance designed with the low-income segment in mind. Whether termed 'mass' insurance, as in many Latin American countries, 'solidarity' insurance (Venezuela) or 'popular' insurance (Brazil), the cross-cutting element of what we refer to as 'microinsurance' in this call is a category of products and distribution avenues intended to provide access to insurance to the 'low-income', 'excluded' or 'underserved' market segment. Clarity on what is being defined is key for developing an appropriately demarcated definition to which an exceptional regime will apply.

→ Regarding the why, the objective for establishing a microinsurance definition is directly related to the target itself. There are three main reasons for defining 'microinsurance.' (1) A regulatory definition provides clarity on what 'microinsurance business' is. It delineates microinsurance from other business lines because of the priority to promote access to insurance for the low-income population. Such delineation is pushed by governments when seeking to enable business to reach the unserved population with insurance. (2) Demarcating 'microinsurance' is key for establishing the type of business that allows for differential regulatory treatment. Differential treatment enables incentivising the industry with regards to a flexible regime, allowing alternative distribution channels or adapting certain compliance requirements, in addition to improving consumer protection for the targeted population. (3) A regulatory definition allows setting proportionate requirements for the business line that are adequate for this innovative type of business. These requirements can either be lighter, such as a different product registration process, or more strict, such as requiring shorter claims processing times.

Key elements that should be incorporated into the definition include:

- **A general description of what microinsurance is** – in qualitative and/or quantitative terms[1]
- **The intended client groups** – e.g. the 'low-income segment' or the 'underserved' in general; avoid a narrow definition of the target group[2]
- **The business of microinsurance** – e.g. to tailor prudential requirements to lower risk business
- **The microinsurance underwriter** – allow those who should be viable and do not exclude conventional insurers
- **Microinsurance agents or distribution channels** – their expertise should be commensurate with the advice to be given, which depends of the type of products that they can distribute; require proportionate training and lighter licensing requirements
- **The microinsurance product**, which has to be simple and could be in many classes, e.g. life, nonlife, personal, family, commercial
- **The microinsurance contract**, which should be simple with reduced exclusions; limited contestability for misstatements; include the ability to combine various types of coverage

It should be noted that there are more elements supervisors may want to consider when defining microinsurance business, for example effective and accessible grievance mechanisms. Sometimes these additional elements could be included in a regulatory framework from the beginning, but they can also be added in incrementally by other regulations that are issued later.

Quantitative definitions

For most jurisdictions, a quantitative limit is a core element for delineating microinsurance. Annex A presents six jurisdictions that have set quantitative limits to show the various options and trends.

All but one country – Ghana, which is presented later as case study – has opted for a quantitative limit. From those who use a quantitative definition, all have used the insured amount as a benchmark to identify microinsurance. These range between approximately 3,000 USD and 11,000 USD.

In addition to the cover, three jurisdictions introduced a premium limit, setting a monthly premium between 3.3 USD (until 2009 in Peru), since May 2016 5.1 USD[3] ; 7.5 USD (since 2015 in India) and 25 USD (since 2013 in Phil).

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1 See Annex A for examples of setting quantitative limits, defining the target market and of qualitative elements utilising the SUAVE principle.

2 Some of the countries use quantitative thresholds to determine who can be considered as the target market of microinsurance. This is in some cases determined by the daily wage or the socio-economic group to which the consumer belongs. See Annex A for examples of quantitative limits set to determine the target market.

3 2 percent of the minimum wage which is pegged at 850 PNE (Peruvian Soles), equivalent to 255 USD (OANDA 7.7.2016)

In general there is a trend to set higher amounts both for the insured amount and for the premium. (Note that the IAIS clearly recommends "to set quantitative limits at the highest possible level"[4]). Malaysia, in their recent discussion paper[5] of microinsurance/microtakaful (see below), has also opted to avoid a quantitative definition.

Complementary Actions of the Supervisory Authority

Having considered the objectives and key elements for a microinsurance definition, which is a core element of any new microinsurance regulation, the key regulatory elements can be developed, where a proportional treatment is intended, such as distribution, products or disclosure.

- The question also turns to what actions the supervisory authority should consider once a specific regime is created. These complementary actions are extremely important because when demarcating this business the supervisor must ensure that the regulation is effective in practice.
- To achieve this, it is expected that the supervisory authority adjust their tools and techniques, which could require: a different product approval process and registry; a separate reporting requirement and monitoring system; and innovative approaches to oversee compliance of market conduct rules of distribution channels, such as coordinating with other regulatory entities (e.g. telecomm authorities).
- The supervisor may also need to issue additional guidance or even adjust other regulations that simply no longer fit, for example the fee structure for supervision, sanctions or the compliance of AML, Know Your Customer (KYC) requirements.

Q: Why should regulators and supervisors proactively engage in developing appropriate regulatory frameworks and adapt supervision techniques given the amount of structural changes in the authority and the financial investment required?

If we look at the motivations of the jurisdictions that have already adopted microinsurance regulation, or that are on the way to do so, we can see that generally there are two broad arguments for the development of appropriate regulatory frameworks: (1) a political emphasis on inclusive insurance and (2) a need to effectively protect consumers. The political argument seeks to move forward public policies aiming to enable access for the unserved or underserved, who may otherwise not have access to insurance. Moreover, increasingly, the push for inclusive insurance fits into wider non-financial agendas such as poverty alleviation, improving food security or mitigating the effects of climate change. The consumer protection argument dovetails the increasing trend that supervisors have begun looking beyond the prudential side to focus on conduct of business elements, aiming to protect the first-time insurance consumer.

Access to insurance should be put high on the agenda, and supervisors should seek additional financial and staff resources to realise this imperative. While it is understood that promoting inclusion requires

4 IAIS Application Paper on Regulation and Supervision supporting Inclusive Insurance Markets (2012)
5 Bank Negara Malaysia Microinsurance and Microtakaful Discussion Paper (2016)

considerable resources on the side of the supervisor, it is important that supervisors embark upon regulatory interventions that can provide quick wins, and thus progress incrementally towards an appropriate regulatory framework in the medium term, beginning with the most important regulatory barriers and supervision techniques. It is also important that supervisors consider their own institutional capacities and establish appropriate coordination mechanisms with other authorities, as well as engage in dialogue with the industry for the implementation of a sound regulatory framework for microinsurance.

Challenges and Recommendations

When developing a definition, careful consideration is needed to effectively strike a balance between protecting the consumer and allowing the necessary innovations with a clearly delineated regulatory window for microinsurance.

It is important to be wary of possible faults in design that could lead to unwanted negative consequences. Examples of flaws in definitions could include:

- When **quantitative limits are too low:** the industry could be less motivated to avoid making the investments needed for developing new products and structuring new partnerships, as the margins in this low-cost business are small and return perspective may simply be too low. As such, insurers could end up not engaging in this business altogether, offering products that do not have sufficient value for consumers and clients may get inadequate or no coverage at all.
- **Product characteristics could be too stringent:** this could lead the industry to avoid registering products under the specific framework because they perceive the requirements as being too strict. Such rigidity could leave insufficient flexibility for innovation, making the industry unmotivated or altogether unable to comply with the rules.
- **Insufficient consideration of other regulations and options to distribute or register products:** sometimes other regulations haven't been sufficiently considered when a specific regime is created around the 'definition.' Thus the new regime could end up competing with other regulations that provide more flexibility or concessions in terms of product requirements or permitted distribution channels—these are elements that could lead to potential regulatory arbitrage and consumer protection concerns.

In summary, the negative consequences of a faulty definition could be that:

- **The industry is not incentivised** to innovate and offer products with value to the low-income population
- The exceptional **regime created is not used**
- **Regulatory arbitrage** occurs with other applicable regulatory frameworks
- **Consumer protection** is deficient, and there are market conduct failures in a domain characterised by a vulnerable consumer

So What is Required?

Based on the above, we can conclude on some elements that should be considered when supervisors are planning to create an exceptional regime for microinsurance that will be demarcated by a regulatory definition.

- Firstly, it is important to strike the balance between flexibility provided by certain concessions and obligations by considering the business and the entire regulatory framework, including aspects such as reporting burdens, consumer protection requirements or allowing the use of technology to facilitate processes.
- Secondly, it is key to introduce a definition that is flexible, and consider whether a quantitative limit is really needed. Moreover, not all product criteria and verification tools need to be set in the regulation but can be defined jointly by the industry and supervisory authorities.
- Third, the supervisor needs to set up adequate supervisory tools and techniques adapted to the specific business line, keeping in mind the importance of consumer protection. This could be done by establishing a separate monitoring system with the support of other authorities, verifying products through innovative processes and supervising non-traditional distribution channels.
- Lastly, it is key that the supervisor is flexible, as this is a very dynamic market where constant monitoring and engagement in dialogue with the industry is required. A flexible attitude will allow supervisors to respond to new challenges, update regulation and supervisory tools as required and to complement regulation with guidance.

Case Studies – Peru and Ghana

The following two country examples shared on the calls from Peru and Ghana, respectively. Bank Negara of Malaysia also shared their experience with developing a microinsurance definition via email.

Peru

The case of Peru illustrates the importance of a flexible approach to ensure regulation is regularly updated to promote the development of the microinsurance market.

Since 2007, the Superintendencia de Banca, Seguros y AFP del Peru (SBS) has been actively involved in improving their microinsurance regulatory framework in response to changes in the market as well as industry input. Peru has ratified two regulations on microinsurance, one in 2007 and the other in 2009, and has adopted a new regulation that builds on elements of the two former legislations issued on 24 May 2016.

In 2007, the SBS introduced a regulation that provided a differentiated regulatory regime for microinsurance in the low-income space. The 2007 Regulation had three key elements that were tailored to the target market: (1) simple insurance with few exclusions, (2) low-cost insurance that had quantitative limits to the insured amount and premium, and (3) the allowed use of new distribution channels—this being an important industry incentive. While the regulation drew the attention of the industry, certain elements of the regulation were found to restrict innovation and thereby client value.

The Superintendence responded in 2009 by identifying these elements and amending them accordingly. This entailed establishing a more accurate but also wider definition of microinsurance that abolished the quantitative elements and included qualitative parameters; including more specific characteristics tailored to added value; requiring broker identification; removing the quantitative limits to amounts insured and premium caps; and amending regulations on premium payments and contract cancellation options for insurers.

While these improvements advanced market development, much microinsurance was still registered under other lines. In May 2016 a new regulation making further improvements was adopted. This new regulation foresees the universal application of regulation to all products meeting the characteristics identified for 'microinsurance'. The most important changes relate to: an updated definition requiring that products meet the elements described for the target audience and a reintroduction of premium limits (see footnote 3); a more flexible product registration process (file and launch within 15 days); a longer deadline for claims payments (20 days instead of 10); allowing the use of electronic sales and policies; the requirement of disclosure of commission and training agents of commercialisation channels; and appropriate disclosure.

In addition to the current regulation, Peru has two new microinsurance projects on the horizon. The SBS is planning to adopt a national financial inclusion strategy that focuses not only on the access to but also the usage of insurance. In tandem, the SBS is launching an initiative to create a detailed microinsurance action plan. The plan builds on the implementation of the new regulatory framework for microinsurance, encourages the use of innovative channels, facilitates new product development, promotes standardised policy conditions, incorporates insurance into social programmes and develops financial inclusion indicators to enable sound monitoring.

Ghana

The case study of Ghana outlined the steps taken by the National Insurance Commission (NIC) to develop a microinsurance regulatory definition. The objectives, process, key elements, challenges, results and future plans involved in establishing Ghana's rather unique qualitative definition were discussed.

Objectives

The NIC developed a regulatory definition for microinsurance with the ultimate objective to provide legal certainty—both for providers, i.e. insurers and intermediaries, and for the supervisory authority—as well as to clarify what microinsurance is and what it is not. Establishing a definition clearly delineates a separate regulatory framework for the 'microinsurance' business line. By having a clear definition of which products qualify as microinsurance and which do not, the NIC is able to effectively monitor progress in microinsurance market development and to minimise ambiguities that enable regulatory arbitrage.

Process

It was a long journey towards developing a regulatory definition for microinsurance in Ghana. The NIC first began by examining pre-existing definitions from many other jurisdictions, studying what others had done and learning from relative successes and failures. Throughout the entirety of the process the NIC involved the industry and other relevant stakeholders – e.g. microfinance institutions (MFIs), NGOs and state ministries – in order to include a wide range of perspectives and ideas. Collectively establishing the definition took about two years. To support implementation, the NIC relies on three legal instruments: (1) Market Conduct Rules legally outlining the position of microinsurance, (2) an Explanatory Note explaining what these rules entail as well as (3) a Guidance Note on how to comply with the regulation in practice.

Key Elements

There are three main elements the NIC used to craft their definition of microinsurance. The first regards the target client group. According to the NIC's definition, the product must be designed specifically to meet the needs of a specific target market, i.e. focusing on the low-income segment, although others may also be allowed to use the product. Second, the product must be affordable for the low-income target market. For this assessments were and continue to be undertaken. Lastly, the product must be accessible. For this element the NIC specified the importance of utilising distribution channels that make the product available, focusing both on the feasibility of using a specific channel as well as the channel's cost effectiveness.

Challenges

As with any implementation process, the NIC came across some challenges when establishing their definition. Firstly, there was ambiguity within the industry when it came to discretion of the three 'microinsurance' criteria that had been set—target group, affordability and accessibility. The product proposals from the industry were extremely wide-ranging in terms of what they regarded as meeting the key requirements. In response, the NIC decided that the industry needed more guidance and thus issued the Written Record of Assessment. Developed in a workshop with the industry, the Assessment Record is a supporting document filled out by the industry to provide proof of compliance with the given assessment criteria.

Results

According to a 2014 Landscape Study conducted on the state of microinsurance in Ghana, 13 out of the 48 conventional insurance companies offer microinsurance products. There are currently no companies that exclusively market microinsurance. Twenty-seven active products have been registered and are developing well on the market so far. Concerning coverage, almost 30 percent of the population – 7.5 million people – have been covered by microinsurance as of December 2014, many of them by digitally supported distribution.

New Plans

Moving forward, the NIC has devised new plans for enhancing the state of microinsurance in Ghana. Specifically, they plan to create conditions for easier access to microinsurance by a wider scope of the population, to improve product approval speed and to lower product registration fees from 2000 GHC to 300 GHC, among others. Additionally, recognising that the largest distribution channel in Ghana is the mobile phone, the NIC plans to remove some of the barriers limiting its use whilst simultaneously addressing the risks and consumer protection challenges inherent to utilising this medium.

Malaysia

Bank Negara of Malaysia also shared their experience with designing a microinsurance definition. Malaysia is currently working on a microinsurance and microtakaful regulatory framework, which was recently issued as a discussion paper. Bank Negara has intentionally used a descriptive and outcome-oriented rather than a strict quantitative definition. This is due to the relatively little industry experience with microinsurance or microtakaful in the country; there are currently only a limited number of products on the market. Given the lack of supporting data, Bank Negara has chosen to forego a quantitative limit for fear of unintended exclusion of target groups. Oriented to the intention of inclusive insurance, "A microinsurance/microtakaful product is an insurance/takaful product that is designed to respond to the financial protection needs of low-income households." This definition is used as a basis for their regulatory approach which is based on case-by-case product approval.

Questions and Discussion

Based on practical experience, is there any call for redefining Ghana's definition of microinsurance?
Martina Wiedmaier-Pfister, speaking on behalf of Kofi Andoh from the National Insurance Commission (NIC) Ghana, stated that the NIC is very satisfied with the open definition they have adopted. While adjustments have been made, they have been geared towards enhancing the NIC's own capacity to assess products, on a case-by-case basis, within the framework of three broad criteria: (1) meeting specific needs of the low-income segment, and their (2) affordability and (3) accessibility. The NIC believes that this approach has enabled them to better protect consumers due to the strict requirements and ensure that products registered as 'microinsurance' have client value. Thus, the NIC seems very satisfied with the open approach they have been taking and sees no specific need to adjust their definition.

Martina then added her own commentary about the need for flexibility of the supervisory authority, observing that new trends in a given market may require supervisors to modify their definition and that monitoring and data analysis is very important to check up on the development of microinsurance volumes and quality early in the process.

Martina also noted that the use of new technology has generally not been included within microinsurance regulations of the past decade. Yet given the move towards digitalisation, updating the regulatory framework is very important. For example, the Philippines has issued at least 20 different regulations and their microinsurance definition has been changed three times, making it more open in terms of the quantitative amount. In contrast, India has had the same regulation in place for the past decade and revised it last year.

Her plea to supervisors is thus to watch closely, to monitor and to adjust the regulatory framework to ensure that the issued framework is actually being used.

Can regulators force insurance companies to declare certain products as microinsurance?
Michael Kofi Andoh explained that in the case of Ghana, all products must be approved by the NIC before commercialisation. While there are concessions and flexibilities to encourage the microinsurance business line, the NIC has laid out clear guidelines on what the requirements of microinsurance products are. This incorporates market conduct rules in order to protect the low-income segment, which tends to be characterised by lower levels of education and financial literacy, and to ensure products have good value for the target client. Even if a product qualifies as microinsurance, registering it as such depends on the segment of the population that it is being marketed to. So when a product falls into the low-income target group, because of consumer protection requirements the company will be required to designate the product as microinsurance.

Andrea Camargo added that in Peru, the SBS came across cases where companies were telling their consumers that a product was microinsurance when in fact it was registered as a mass insurance product. The SBS has two completely separate sets of consumer protection regulation for each product line. Thus when customers purchase microinsurance products that are actually registered as mass, they are unable to have the very benefits that were designed to protect them and offer value (e.g. rapid claims settlement and complaints resolution, or few exclusions). These kinds of problems illustrate the importance that regulators hold the industry accountable to properly demarcate products and avoid issues of consumer protection.

Did Ghana witness any improvements in insurance penetration after introducing microinsurance?
Insurance penetration is the percentage of gross insurance premiums to a nation's GDP. Since microinsurance premiums are actually quite small, in Ghana there has not been much impact on penetration yet. This is something, however, that is expected to happen sometime in the future, as nurturing today's microinsurance market may allow it to become part of tomorrow's conventional insurance market. Even though there is not much impact yet on penetration, there has been a tremendous impact on the number of lives covered by (micro)insurance. In Ghana the number of lives covered by microinsurance has increased from 1.7 million in 2011 to 7.5 million as of December 2014.

Why was there a necessity in Peru to identify and tackle the topic of commercialisation?
Carla Chiappe of the SBS explained that in Peru many (microinsurance) products were registered but never commercialised. In order to address this tendency in 2009 it was decided that the insurer from then on had to indicate how the product was to be commercialised when registering it with SBS.

How did the SBS define what "few exclusion" means?
The SBS revises exclusions but there is no generally accepted definition of what "few" is. It is, however, common understanding that a microinsurance product should have only product-related exclusions that are unavoidable for an insurer (e.g. war, etc.).

Annex

Annex A

Table 1: Examples of quantitative limits[6] (in USD) and defining a target market

	India	Philippines	Peru	Pakistan	Brazil	Ghana
Quantitative Limit						
Insured Amount	80-800 (2005) 3,500 (2015) life; varies for other products	4,000 (2006) 4,200 (2010) 11,000 (2013)	3,300 (2007) None (2009) None (2016)	Depending on the type of product (5-40 times the minimum monthly wage)	Depends on the type of product (14-17,400 USD)	None
Insurance Premium	90 (2015) annual for life	10/5/7.5% of the daily minimum wage	3.3 (2007) None (2009) 4.5 (2016)	None	None	None
Defining Target Market						
	Low income population	Low income population	Low income people and micro-entre-preneurs (no quantitative benchmark)	Person with monthly income less than the minimum taxable income or as set up by the commission	Low income people and individual micro-entrepreneurs 'Low income' defined as a person with a monthly income less than 2 minimum wages	Low income people, specific types or descrip-tions of low income persons, or low income persons in a particular geo-graphical area

Annex B

Examples of Qualitative Elements: The SUAVE[7] Principle

The SUAVE criteria provide a valuable framework for identifying the most important qualitative elements of microinsurance definitions. Microinsurance products and processes should be:

→ **S**imple
- Product design (simple covers, no or few exclusions)
- Subscription process (contract, adapting AML/KYC[8] requirements)
- Policy documents (transparent, local language, colloquial terms)
- Claims processes

→ **U**nderstandable
- Tailor-made education tools, training for channels

6 The IAIS, in its application paper, recommends setting quantitative limits at the highest possible level.
7 Microinsurance Centre (2011) "SUAVE Checklist for Microinsurance Products: Enhancing the potential for success"
8 'Anti-Money Laundering/Know Your Customer'

→ **A**ccessible

- Distributed by channels which consumers have easy access to, information available in a timely manner, consumers able to receive the benefits

→ **V**aluable

- Product responds to the needs of the clients, the price is fair, rapid claims

→ **E**fficient – for both providers and consumers

- Claims process, premium payment, complaints handling
- Allow the use of technology to facilitate processes (e.g. electronic signature, remote subscription, mobile payment)
- Allow the use of group subscription ensuring effective consumer protection for insured parties

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