Report of the 5th A2ii – IAIS Consultation Call

Product Oversight in Inclusive Insurance

28 August 2014

In situations where access to insurance markets is very limited, conventional product design may not be sufficient to overcome barriers to access. In these cases, product innovation can help reach potential consumers by making products and services attractive and affordable, while remaining economically viable. Given the opportunity and risk in product innovation, finding a suitable regulatory approach to product oversight becomes a crucial means of achieving a jurisdiction's regulatory objectives.

The **fifth consultation call** in the **consultation call series** focused on product oversight in inclusive insurance. The call was held on Thursday August 28 and was attended by over 40 participants from across Asia, Africa, Latin America and North America. The experts on the call were Michael Hafeman and Martina Wiedmaier-Pfister. Country experiences were shared by Sriram Taranikanti (India: IRDA), Jacky Huma (South Africa: FSB), Alexandra de Jong (Europe: EIOPA), Eric Nordman (USA: NAIC), Regina Simoes / Maria Alves (Brazil: SUSEP) and Kofi Andoh (Ghana: NIC).

The role of product oversight

Product oversight has a crucial role to play in achieving regulatory objectives such as promoting fair treatment of policyholders, reducing the risk of insurer failure and encouraging innovations that enhance access.

Successful product oversight approaches weigh risks and mitigants[1] appropriately for a jurisdiction. Risks include: inappropriate new products (do not meet consumers' needs, are excessively priced, or have inappropriate policy provisions); operational risk; and untested approaches in marketing, distribution, premium collection, etc. Such risks need to be managed by insurers and assessed by supervisors.

A number of mitigating conditions should be reviewed to assess how tightly the regulator needs to control product oversight. These conditions include reviewing the technical capacity of insurers, their in-house product development and market conduct, the capabilities of the distribution system, consumers' familiarity with the products and the oversight capacity of the supervisor. As far as possible, assessment of product risk should be effected by insurers themselves, with the supervisor maintaining an oversight role.

The regulator is able to determine the best product oversight approach by weighing risks and mitigants in the light of regulatory objectives. Where risks are high and mitigants weak, a pre-approval process will allow the supervisor the highest level of control. Where risks are low and mitigants strong, it is sufficient for the supervisor to monitor. In between, the supervisor may find that the balance of risks and mitigants makes file-and-use the most suitable regulatory approach to product oversight.

The role of product oversight when building inclusive insurance markets

Jurisdictions that are building inclusive insurance markets often have to navigate a different environment of mitigants. Insurers in these jurisdictions might have limited technical capabilities and, additionally, are facing a new market segment. The effect is that often only a small share of registered microinsurance products is marketed effectively and produces sales at scale. Additionally, the business model may have only limited market conduct oversight, given that some of the innovation may occur in distribution. New distribution channels, such as non-banking agents, retail shops or utility companies, are often outside of the regulated insurance sphere. They may involve large numbers of agents which might have a high drop-out rate. Insurers need time to develop and effectively implement new control approaches that take into consideration the particularities of these channels.

Similarly, the novelty of inclusive insurance products may affect the supervisors' ability to register products and supervise this business. When supervisory staff is new to microinsurance, they first have to learn more about the products and distribution approaches. This may cause significant delays in product approval, affecting the willingness of industry players to enter the market

[1] Definition of mitigant: Something mitigating, a means of easing, lessening or assuaging

or develop products that will better serve currently underserved customer segments.

On top of these challenges, building inclusive markets often means dealing with first-time insurance customers. Their lack of familiarity with the products tends to be low, and normal levels of disclosure may not be understood. Customers may not have the resources or knowledge to seek remedies for inappropriate products. And because they are first-time buyers, a bad product experience may make the customer unwilling to buy insurance again.

Country context for addressing product oversight

India (Insurance Regulatory and Development Authority, IRDA)

India sees product design as a critical component of market conduct regulation, with specific relevance to inclusive markets. The low income segment generally has limited financial education. Therefore, the microinsurance regulatory framework defines product parameters such as risk coverage (sum assured) and only certain product categories are allowed.

Expansion into the rural and social sectors is incentivized through specific take-up targets for each insurance company. More recently, such products are being sold through 125,000 state supported Common Service Centres. Given the higher cost to serve the targeted poorer customers, regulations allow for higher remuneration to intermediaries and allow insurance products to be linked to other services at the customers' doorstep. To foster market expansion, the IRDA seeks to be liberal in its licensing process and commission limits. Consumer protection needs are balanced with seeking to extend financial inclusion. At present, the range of microinsurance products remains relatively limited, representing 14 out of a total of 500 life products, 95 out of 2,300 non-life products and 16 out of 566 health products. However, it is open for the inclusive segments to buy as per their choice from the mainstream insurance products which are also on the offer and accessible.

Product design guidelines are issued specifically for microinsurance and insurance products targeted at rural / social sectors. Amongst other requirements, products have to meet actuarial scrutiny and comply with regulations, including simple language in policy forms and sales literature. Products have to meet certain features, such as being simple and inexpensive, easily understood, have reduced distribution costs and focus on product lines that are bought rather than sold. These requirements are validated through a **file & use** system, where products are reviewed by Product Approval Committees consisting of actuaries and subject matter experts, with every approved product receiving a unique identification number. Regulations are currently under review to introduce further safeguards to protect vulnerable customers.

South Africa (Financial Services Board, FSB)

South Africa's microinsurance policy proposals[2] tightly control the parameters of product design permissible under a microinsurance license, in order to balance consumer protection and market growth imperatives. Product review will take place on a **file & use** basis.

In South Africa's policy proposal, microinsurance products are defined as risk benefits only, with no surrender value. Savings components are not allowed. Under the microinsurance line, benefits are capped for death events, other risk events (accident and disability) and asset insurance.

Microinsurance products are limited to a maximum product term of 12 months, at which point the product can be renewed. Underwriting can be applied either on an individual or group basis, and waiting periods are limited to a maximum of six months for death and disability products. Accidental death products cannot apply a waiting period. Exclusions may not be enforced for pre-existing conditions and, in life policies, exclusions with respect to suicide may apply for only two years. A right to a monetary benefit without administration fee is required to enhance the value of the product to the customer. For

[2] Proposals discussed refer to policy proposals published in July 2011, which are going to be enacted as part of a wider Conduct of Business legislation under the Twin Peaks regulatory framework which will soon be introduced in South Africa.

the same reason, microinsurance claims should be paid within 48 hours of receipt of the requisite information, and in respect of grace periods, customers have the right to same terms reinstatement, with the contract being reset to one month after reinstatement. To lower the costs of business, the regulator will permit initial pricing and subsequent changes on policies to be signed off by an actuarial technician, rather than a full actuary.

Europe (European Insurance and Occupational Pensions Authority, EIOPA)

In Europe, the supervision of the insurance sector is carried out predominantly by the National Supervisory Authorities. EIOPA's role is among others to promote the convergence of supervisory practices[3]. To this end, EIOPA works jointly with the 31 European supervisors[4] to develop standards, which can be then implemented at national level. European supervisors apply a **monitoring** approach to product oversight; product pre-approval is not allowed in European law.

However, since early 2014, product oversight has been an issue under consideration due to consumer protection concerns and in order to facilitate convergence of supervisory practices across Europe. Namely, at present only four EU Member States have product oversight requirements in place.
To address this issue, EIOPA is currently focusing its attention on the activities of insurance undertakings as manufacturers of insurance products. The results of their work will be open to public consultation in Q4 2014 and will be available at EIOPA's website. At a later stage, EIOPA may turn to reviewing distributors.

The foundation for EIOPA to develop Guidelines on product oversight and governance arrangements by insurance undertakings can be found in high-level principles for banking, securities and insurance sectors. Further details on these high-level principles are available at EIOPA's Joint Committee website.

[3] For further details about the role and tasks of EIOPA, please consult the EIOPA founding Regulation (available at http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2010:331:0048:0083:EN:PDF).
[4] 28 EU Members States as well as Iceland, Liechtenstein and Norway.

USA (National Association of Insurance Commissioners, NAIC)

Similar to Europe, the USA locates insurance regulation at the state level, i.e. there are 56 independent insurance supervisors. The US market is large compared to most others, with 50 US jurisdictions falling amongst the top 100 globally by premium volume. To give a further sense of scale, 648,150 product filings were submitted and processed electronically through the NAIC System for Electronic Rate and Form Filing (SERFF) (2013 figures); 1,200 people are responsible for some aspect of product review; 500 people are involved in market conduct regulation, including post-reviews of product filings; and 2,600 people are involved in handling consumer complaints and enforcement. SERFF is run centrally on behalf of individual states and tracks 7,500 insurers.

Approaches to product oversight are uniformly driven by consumer protection laws and regulations. Policy forms are reviewed to ensure that they meet the minimum requirements of state consumer protection laws and regulations, deliver expected benefits to consumers, and do not contain misleading or deceptive provisions to disadvantage the consumer. In the general case, insurance regulation in the USA is simple, as long as insurers treat customers properly, i.e. meet claims and do not mislead or cause another form of disadvantage.

Jurisdictions **vary widely** in their approach to product oversight, including using prior approval, file & use, use & file, flex rating (i.e. file & use unless rate changes are larger than a specified small band; if the change is larger, then prior approval of pricing is required), informational filing, filing of a list of current policy forms, and no filing. These approaches stem from different regulatory philosophies. For example, prior approval helps eliminate unfair methods of competition and reduce deceptive business practices before a product is sold to the public. On the other hand, file & use or use & file helps insurers with speed to market and protects consumers by providing for withdrawal of approval if products do not meet regulatory requirements.

A number of considerations are looked at when reviewing "good practices" in policy form review. For example, supervisors verify whether the policy forms an insurance contract, whether the insurer is licensed to offer this line of business, whether the product contains an acceptable risk transfer and whether the insuring agreement contains a clear and concise statement of what the insurer is offering to the policyholder.

Brazil (Superintendencia de Seguros Privados, SUSEP)

The Brazilian supervisor oversees 8,515 products by 162 supervised insurance companies at present. Product oversight varies by product line. For general insurance, file & use is applied, meaning that products are approved for launch after SUSEP performs a quick analysis and releases the product registration number to the insurance company. For life insurance lines with a saving component, approve & use is applied, meaning that prior approval is required before the product can be marketed. For microinsurance lines, **file & use** is applied.

At present, SUSEP provides product oversight for 30 microinsurance products and 16 insurers offering microinsurance. On average, product approval is obtained in three days as long as the product operates with standardized coverage and exclusions as per the microinsurance regulation.

Quick turn-around of product oversight is facilitated by use of an electronic, web-based system. Insurance companies upload their products to the system and after Susep performs a minimum checklist on it, the product information is publically accessible on the SUSEP website. This procedure is an important transparency tool since it allows consumers and other stakeholders to check if the insurance policy sold is in accordance with the product registered at SUSEP. The system is linked to a statistical accounting database, allowing information such as market share, claims ratios, and premiums by line of insurance to be retrieved. It enables SUSEP to have control and full visibility of all insurance products and a better view of the supervised market, since its control is not only limited to the insurance policy itself, but also allows SUSEP to have a global view of the product performance in the market.

Ghana (National Insurance Commission, NIC)

Insurance products in Ghana can only be issued after the NIC has given its **prior written approval** for the product. This approach is taken given that the local insurance market is still developing, with consumer protection understanding in its infancy. Most of the population is unfamiliar with insurance, so the regulator ensures that products deliver value. A new law is currently being passed that will allow for a file & use approach to product oversight. In the meantime, transitional prior approval rules apply.

Insurers apply for new product assessments by submitting a policy contract, an actuarial estimate and a written record of assessment (indicating how the target market, price, affordability and accessibility of the product were assessed internally).

In Ghana, microinsurance is defined as targeting a certain market segment. This segment must be proven to be low income generally, or a specific type or description of low income, or a low income person limited to a specific geographic area. Premiums must be affordable to the target market, and the insurance contract must be readily understandable to customers. However, microinsurance products can also be purchased by higher income customers.

Microinsurance in Ghana faces a number of challenges. Amongst others, Ghana has a shortage of actuaries and the regulator needs to coordinate with other governmental bodies, such as in health insurance (the partnering regulator being the National Health Insurance Authority). Stakeholders find the regulations defining microinsurance to be vague, even though the definition was intentionally vague in order to leave room for innovation. Finally, new forms of products require new regulatory approaches. For example, mobile insurance can be bought inadvertently when clients buy airtime, as an add-in package. For the moment, the regulator is still assessing how to protect these mobile insurance consumers, who may not be aware that they own cover.

Closing thoughts

Regulators level of product oversight is driven by specific regulatory objectives and a proper weighing of risks and mitigants related to the product. Country examples shared in this briefing span a wide range of approaches taken to product oversight, depending, amongst other things, on the maturity of the insurance industry and the level of supervisory capacity.

Access to Insurance Initiative
Hosted by GIZ Sector Project Financial Systems
Approaches to Insurance
Gesellschaft für Internationale
Zusammenarbeit (GIZ) GmbH
Dag-Hammarskjöld-Weg 1-5
65760 Eschborn, Germany

Telephone: +49 61 96 79-1362
Fax: +49 61 96 79-80 1362
E-mail: secretariat@a2ii.org
Internet: www.a2ii.org

The Initiative is a partnership between:

Hosted by: