access to insurance initiative

IAIS
INTERNATIONAL ASSOCIATION OF INSURANCE SUPERVISORS

Report of the 2nd A2ii – IAIS Consultation Call

Technical innovations in insurance distribution and regulatory implications

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When insurance markets are less accessible to a group of customers, conventional approaches may not succeed in overcoming the barriers to access. In situations where access to insurance markets is impeded, technical innovation can help reach potential consumers by making products and services attractive and economically viable. For example, in recent years m-insurance (insurance sold through and/or with a mobile network operator (MNO) has gained attention due to its rapid growth in many insurance markets and its potential to advance inclusive insurance.

Regulation and supervision needs to permit these approaches while protecting policyholders to facilitate this growth. Regulation should recognize a wide range of business models, potential market participants and service providers while ensuring a safe, fair and stable insurance market. The IAIS Application Paper on Regulation and Supervision Supporting Inclusive Insurance Markets (IAIS, 2012) suggests several criteria for these technical innovations. These include that insurance should be formal, innovations need to be facilitated, roles and responsibilities need to be clear, and a proportionate approach is recommended. The recently released synthesis papers on business models and regulatory approaches, commissioned by the A2ii, provides some additional regulatory responses. However, given the speed at which technical innovations in insurance distribution are being deployed, regulators are interested to know the most recent developments in this area.

The **second consultation call** in the **consultation call series** focused on technical innovations in insurance distribution and regulatory implications. The call was held on Thursday April 24 and was attended by 26 participants from across Asia, Africa, Latin America and North America. The experts on the call were Hennie Bester, John Owens and Jeremy Leach.

The call was opened by Peter Braumüller, Chair of the IAIS Executive Committee, who highlighted the IAIS' support for the call: *„Only through learning and understanding where we (IAIS members) are, the problems we see, where we want to go, can we try to provide solutions together."*

Technology and business models in insurance

The A2ii commissioned two synthesis papers based on an analysis of all the A2ii country diagnostic studies and several other studies and microinsurance regulatory frameworks, considering 25 different jurisdictions in total. The first paper identified eight distinctive business models and their associated consumer protection risks, as well as potential regulatory responses. Two of these models in particular, auto-enrolment and proxy sales force, utilize mobile phone technology more than the others. Auto-enrolment is when a third party purchases insurance on behalf of a pre-determined group of people. The third party, in this case the MNO, prescribes the product and subsidizes, sometimes in full, the premium in exchange for customer loyalty. The proxy sales force business model is utilised when insurance is sold by a non-insurance entity with a large client base and non-insurance sale force, such as an MNO, to existing clients. In some cases, sale and premium collection are automated, via a drop-down menu on a mobile phone, while in others there is some human interaction. There may also be case where the insurance is included in the subscription package without any interaction with the client.

Hennie Bester explained that both of these business models give rise to discrete consumer protection risks. Auto-enrolment gives rise to policy-awareness risk, where the insured is not aware he or she has an insurance policy and is therefore unable to lodge a claim. Generally, this is accompanied by very low claims ratios. To respond to this risk, regulators may look to increase disclosure requirements or require post-sales communication. Meanwhile, a proxy sales force model gives rise to aggregator risk, where a client obtains no value from the product because the product is not the aggregator's core business. In many cases, the power imbalance between the MNO and the insurer is sufficiently large and the MNO can dictate the terms and link the cover to its own financial interests, rather than the insurance needs of the client. In response, regulators may look to increase disclosure requirements, proactively monitor claims and expense ratios, or require agreements between MNOs, brokers and insurers to be disclosed to the supervisor.

How should banking supervisors deal with oversight of mobile financial services?

The oversight of mobile financial services (MFS) has been a key issue for central banks and other financial regulatory institutions from developing countries. The Alliance for Financial Inclusion (AFI) is a global network of 117 financial policymakers from 94 developing and emerging countries working together to support financial inclusion. AFI's Mobile Financial Services Working Group (MFSWG) promotes the broad use of mobile and other digital financial services as a key solution to improve financial inclusion and provides a platform for policymakers to discuss regulatory issues on MFS. The Group has developed a series of guideline notes[1] for regulators and policymakers, several of which are useful for insurance regulators to review, given that they address the licensing and supervision of mobile insurance services. One of the relevant guideline notes focuses on technology risks in MFS (Guideline Note on Mobile Financial Services: Technology Risks). This note provides five principles that guide regulators in looking at MFS technology risk management: confidentiality, integrity, availability, authentication and non-repudiation. Understanding these five principles guiding MFS technology risk management helps regulators determine and ensure appropriate regulatory as well as supervisory responses.

In addition to these five principles, John Owens shared the following considerations relevant for both insurance and banking supervisors when dealing with the mobile channel. He explained that regulatory coordination may be necessary between telecommunications and insurance supervisors, as well as banking and payment supervisors, especially when mobile money is utilized for payments or disbursements. Some examples of recent collaboration between financial systems regulators and telecommunications regulators include Colombia and Bangladesh. In both countries, telecommunication regulators played a role in setting maximum Unstructured Supplementary Service Data USSD) and SMS fee structures for MNOs to ensure fair access by financial service providers and their clients wanting to use mobile channels. It is also important to define relationships and responsibilities between insurance companies and the other parties involved. In the Philippines, a new mobile banking service provider, BPI Globe BanKO, which offered a new m-insurance scheme, was required to get a microinsurance agent license. This initiated a collaborative process between the Insurance Commission of the Philippines and the Bangko Sentral ng Pilipinas. In addition, as with all other microinsurance offerings in the Philippines distributed through banks, the bank was required to prominently display and notify all clients that the insurance product came from an insurance company and is not guaranteed by the bank. Finally, as noted in the recent AFI Guideline Note on Consumer Protection in MFS, it will also be important for regulators overseeing mobile insurance to ensure that providers are taking additional steps to protect clients. These include the need for clients to be able to protect themselves by being educated on everything from understanding the very basics of what a PIN is, to other aspects that reduce the potential for consumer abuses, such as the process for filing a claim, a complaint, or receiving a remote insurance payment, especially if the mobile channel is being utilized to facilitate this process.

What can go wrong in technical innovations? Lessons learned from an m-insurance failure

The potential for scale in m-insurance brings significant opportunity to increase financial inclusion as demonstrated by several m-insurance 'sprinters'. For example, Tigo Ghana reached almost one million lives in 12 months, Airtel Zambia reached an estimated two million adults at launch and Telenor Pakistan reached over a million lives in six months. However, not all schemes that have achieved scale can be considered a success. Jeremy Leach introduced the case of Eco-Life Zimbabwe. Eco-Life was a partnership between Econet Wireless (the largest MNO in Zimbabwe), First Mutual Life (an insurer in Zimbabwe) and Trustco (a third party technical service provider based in Namibia). EcoLife reached 20% of the adult population within 7

[1] AFI has recently developed various relevant and useful guideline notes on the Supervision and Oversight of Mobile Financial Services (http://www.afi-global.org//library/publications/mobile-financial-services-supervision-and-oversight-mfs-2014) and Consumer Protection in Mobile Financial Services (http://www.afi-global.org//library/publications/mobile-financial-services-consumer-protection-mfs-2014) which are also relevant for those looking at issues around the use of mobile insurance services.

months of launch, but due to a dispute between two of the non-insurance entities, Trustco and Econet, the scheme was discontinued overnight. In undertaking a survey of the discontinued clients of EcoLife, 63% ruled out the use of similar products in future, 42% were dissatisfied with insurance and 30% felt there were better ways to protect against future problems than insurance. Considering the product had reached 20% of the adult population, the impact was significant.

Jeremy Leach explained that at this scale, some m-insurance schemes can have market wide impact and while the dictum „do not rush to regulate" has important lessons for supervisors, there is also a need to set rules ex ante to ensure positive synergy between financial inclusion and a stable and well-functioning insurance sector. To mitigate this potential risk, the business risk framework needs to be extended to include data risk, systemic risk and regulatory backlash risk. Jeremy highlighted seven draft recommendations concerning the regulation of m-insurance from Regulating m-insurance in Zimbabwe: managing risk while facilitating innovation. The core messages for regulators thinking through supporting these models is that they need to make sure that there are minimum conditions in place; that regulators understand the schemes; that the schemes are communicated well; that the risks arising from them are managed effectively; and finally, that the regulator supports the creation of a ‚living will' where the conditions for exiting the scheme are established upfront so that it limits any market wide impact.

Recommendations for enhancing m-insurance while protecting consumers

The A2ii synthesis study did not find any jurisdictions that up until 2012 had introduced m-insurance specific regulation, but did find countries and supervisors that are ready to assist insurers to develop these models. One approach is to support these models through a product approval process. This does not require a comprehensive regulatory framework. Instead it requires the provider to discuss the main features of the product and the process with the regulator and require it to be approved by the regulator. Generally, the best product to distribute through a mass channel covers a risk that is experienced by almost all of the population. In many, but not all, Sub Saharan African countries this might be funeral insurance and in Asia this might be simple health. The product should not require a complex sales process. Thus one of the enabling conditions is the right product choice.

In Brazil, many clients choose to purchase insurance because of their interest in the underlying non-insurance product. Clients are thus willing to take less favourable insurance policies, introducing new risks to these models. There is a similar potential for this risk with m-insurance, where the clients takes less favourable policy terms because they want the services offered by the MNO. Hennie Bester introduced three additional regulatory responses for this potential consumer risk. The supervisor may require a more comprehensive sales process that includes multiple options for insurance policies, introduce a post-sale communications process or necessitate a cooling off period, where the buyer has up to 30 days to repudiate the policy.

To protect consumers, the IAIS Application Paper on Regulation and Supervision Supporting Inclusive Insurance Markets (IAIS, 2012) recommends that people should know they have insurance and people should know when it ends. However, this is more challenging when dealing with complex value chains, such as with m-insurance. Insurance supervisors often struggle with the relationship with the telecommunications supervisor and what their responsibilities are. In the case of EcoLife, the telecommunications supervisor had no objection in launching the product, but was not as involved in protecting the consumer. Meanwhile after the launch, the insurance supervisor found it difficult to hold the MNO accountable. In many of these countries the insurer is in a weak position vis-à-vis the MNO, so without the insurance supervisor playing an active role the insurance company is likely to have little leverage. Supervisors need have a clear view of the value chain and where the power imbalance is.

In Pakistan, m-insurance has been around for a number of years, but take-up has been erratic. It starts with high growth, but retention is slow. Even the 'sprinter' example covers less than 0.5% of the number of mobile subscribers in Pakistan, albeit in a short time span. Major challenges are education and awareness. Clients do not always understand text messages

from mobile companies and mis-selling is common, for example when the amount of sum assured is not always communicated to the policyholder. Regulatory coordination between banking, insurance and telecommunications supervisors is important, but there need to be clear boundaries on who will perform what role and who is responsible for consumer protection.

Regulators should monitor and evaluate the schemes over time to ensure consumers are receiving value for the product. One approach taken in Ghana was to administer a survey to clients of one of the m-insurance schemes on their experience with the product. The survey allowed the supervisor to understand if the sales process is effective and if the clients understand and receive value from the product.

With innovations in insurance moving so fast, supervisors and regulators need to be ready to regulate and supervise, cooperate with other supervisors such as telecommunication and banking regulators and monitor and evaluate the value for clients.

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