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Discussion Paper Consumer Protection in Microinsurance

An input to the Consumer Protection Task Force of the Microinsurance Network

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List of Abbreviations

ADB	Asian Development Bank
ADR	Alternate Dispute Resolution
AFI	Alliance for Financial Inclusion
BMZ	Bundesministerium für wirtschaftliche Entwicklung und Zusammenarbeit (German Federal Ministry for Economic Development and Cooperation)
BOU	Bank of Uganda
CFPB	Consumer Financial Protection Bureau (United States of America)
CGAP	Consultative Group to Assist the Poor
CFPB	Consumer Financial Protection Bureau
CI	Consumers International
CP	Consumer Protection
DFID	Department for International Development
DOF	Department of Finance
EU	European Union
FASECOLDA	La Federación de Aseguradores Colombianos (The Federation of Colombian Insurers)
G20	Group of 20
GIZ	Deutsche Gesellschaft für Internationale Zusammenarbeit GmbH
IAIS	International Association of Insurance Supervisors
ICPs	Insurance Core Principles
ILO	International Labour Organization
IRDA	Insurance Regulatory and Development Authority
KfW	KfW Entwicklungsbank
MFI	Microfinance Institution
MFW4A	Making Finance Work for Africa
MI	Microinsurance
MIN	Microinsurance Network
MOF	Ministry of Finance
MOH	Ministry of Health
NAPC	National Anti-Poverty Commission
NCC	National Credit Council (of the Department of Finance Philippines)
NIC	National Insurance Commission (Ghana)
OECD	Organization for Economic Co-operation and Development
RBI	Reserve Bank of India
RF	Responsible Finance
RSP	Regulation, Supervision and Policy Working Group
SBS Peru	Superintendencia de Bancos, Seguros y AFPs (Superintendence of Banking, Insurance and Pension Funds)
UN	United Nations
UNEP FI	United Nations Environment Program Finance Initiative
USAID	United States Agency for International Development
WB	World Bank

Abstract

Microinsurance markets are growing rapidly. New providers enter the market, offering innovative products and/or employing innovative provider models. Innovations can lead to new consumer protection needs, and also have a tendency to aggravate existing challenges of asymmetric information, market power imbalances and other imperfections that are typical for insurance products in general and are worse when poor and illiterate consumers are concerned. Most low-income consumers are new to insurance and lack trust in the market. Many existing consumer protection frameworks lack consideration of these aspects.

Weak consumer protection can have severe consequences for microinsurance consumers, but also the further development of microinsurance markets as a whole. Issues related to consumer protection in microinsurance are wide-ranging, including financially illiteracy, complexity of insurance products, capacity of (formal and informal) insurance providers, and low trust by policyholders in providers and the regulatory frameworks. With increasing prevalence of microinsurance and numerous national and international stakeholders working on the issue, good and bad practices are beginning to emerge on various aspects of the topic.

This paper suggests a framework for a holistic view of consumer protection in microinsurance. It starts by defining an »ideal insurance process« that puts the consumer in a position to take full advantage of microinsurance. In the real world, this ideal case is challenged by numerous issues concerning the type of risk and product, insurance company and intermediary, as well as regulator and supervisor. These issues and challenges are discussed together with approaches to consumer protection at both the industry and regulatory/policy level.

1 Introduction

Effective consumer[1] protection is an important precondition to advance access to insurance as a sustainable risk protection mechanism. Growing insurance markets that include the low-income population can only mature if strong consumer protection measures are in place and effective for low-income consumers. The implementation of a comprehensive consumer protection agenda, with low-income consumers at the center, requires public and private stakeholders to join hands.

The **Microinsurance Network** (MIN), which represents the international community on microinsurance, has decided to advance consumer protection in microinsurance through its Consumer Protection (CP) Task Force. Its primary objective is to contribute to effective consumer protection in microinsurance through efforts of various stakeholders, which shall be achieved by consolidating and disseminating experiences, and providing guidance on good practices.

1 Literature uses the terms »consumer«, »customer« and »client« interchangeably. We use the term »consumer«, which includes current, prospective, and potential policyholders and beneficiaries.

In furtherance of this objective, this paper presents an input into the Task Force's work by beginning with a clarification of concepts and identification of issues in consumer protection at public and private level.

The paper is structured as follows: Section 2 elaborates the rationale for consumer protection. Section 3 identifies an »ideal insurance process« in seven steps. From a client's perspective, it explores the roles of industry and the public sector in fulfilling the preconditions for the consumer to take full advantage of insurance at all stages along the »process« of being insured. Section 4 looks at challenges to consumer protection through providers (i.e. risk takers, delivery channels) and products as well as their associations. Section 5 discusses challenges in regulation, supervision and policy, i.e. the role of national authorities and different approaches in microinsurance consumer protection. Section 6 concludes.

2 Rationale of consumer protection in microinsurance

Microinsurance markets have been growing rapidly in recent years. Insurance providers and investors are increasingly recognizing the market potential of microinsurance.[2] Further, policymakers at the global and at national level, as well as international development partners, are aware of the potential microinsurance has to reduce the vulnerability of low-income households by protecting them against a wide variety of risks. These risks range from ill health and death to loss of assets, agricultural risk, and life-cycle events such as marriage or old age.

With the **increase in the supply** of different products and the great variety of stakeholders from both the private sector (insurers, innovative distributors such as mobile network operators, retailer or trade unions) and the public sector (central banks, ministries, supervisors) involved in providing microinsurance, effective consumer protection has become a crucial issue. It is the basis for trust, thereby ensuring the sustainability of insurance services and their providers.

Weak consumer protection can have **severe consequences** for clients, but also the further development of microinsurance markets as a whole. **For the consumer**, inadequate protection can lead to further impoverishment. When purchasing an insurance product, the consumer faces a risk that he will not get the payment promised if an insured event occurs. The insurer may mislead the consumer as to the size of the payout or the conditions required to receive it, or it might go bankrupt or otherwise be unable to pay a claim. Prospective consumers, who might already be distrustful of new and unfamiliar financial products, are even less likely to buy insurance where insurers and insurance products have a bad reputation. Existing consumers might drop out if a product or provider does not fulfill expectations or if they see or hear of problems that other consumers face.

From the insurers' perspective, bad business experiences of microinsurance providers will reduce their willingness to focus on the low-income market and limit the chances that they will successfully develop and sustainably offer microinsurance products in future.

Due to the nature of products, clients and business type, consumer protection requires special attention in the area of microinsurance:

- **Consumers** are often unfamiliar with financial products and services including insurance, and their trust in insurance is typically low. Cash-flow fluctuations of low-income households can limit the ability to regularly pay premiums. Low-income households are also more vulnerable to risk as they have limited access to the whole range of risk mitigating tools.
- **Insurance as a risk mitigation product** is often difficult to understand, not only for potential consumers, but also intermediaries or third party administrators. Hence, there is a great potential for misunderstanding, mistakes, or abuse.
- **Most insurers that have traditionally served higher income segments** might not be familiar with the specific needs of low-income clients. The consumer protection-related requirements for traditional insurance products sold to wealthier and better-educated consumers are often

2 Microinsurance, as defined in the 2007 IAIS-CGAP Issues Paper on the Regulation and Supervision of Microinsurance, is insurance that is accessed by the low-income population, provided by a variety of different entities, run in accordance with generally accepted insurance practices. This means that the risk insured under a microinsurance policy is managed based on insurance principles and funded by premiums. Microinsurance covers a broad variety of products, for example, life insurance, funeral cover, health, invalidity, livestock, crop and asset insurance.

inappropriate for the microinsurance market, and should not simply be applied in exactly the same way to microinsurance. On the other hand, informal or mutual insurers know the market well, but often lack insurance and management capacities, which threatens the sustainability and viability of microinsurance schemes. The development of a sustainable business model including its marketing and servicing is a huge challenge for all kinds of insurers.

- **Alternative delivery and a longer value chain** often involve non-traditional aggregators as intermediaries and third-party administrators. Hence, agency incentives can be the main driver of the kind of product and quantity sold. Sales through family and friends and tying and bundling can increase access to insurance, but pose certain threats as they can limit a consumer's choice and mobility.

Weaknesses at policy level, in regulation and in enforcement add to these challenges. Given the newness of this market insurance supervisors in many countries are still unfamiliar with or even unaware of microinsurance business and the practices of formal as well as informal providers.

The **relevance of consumer protection** in microinsurance has been increasingly recognized at global and national level by public and private actors. Protecting consumers of financial services is a challenge addressed by various organizations as part of their **»responsible finance«** agenda. This agenda is based on the concept of three mutually reinforcing pillars, all of which contribute to strengthening, protecting and empowering consumers of financial services: **consumer protection regulation by governments, self regulation by the industry itself and financial capability/empowerment of the consumers themselves**.

Box 1: Global efforts

Global initiatives such as those of CGAP, ACCION International and its SMART Campaign, the G20 Financial Inclusion Platform, the Alliance for Financial Inclusion (AFI), the World Bank, the Organization for Economic Co-operation and Development (OECD), bi- and multilateral donors, and standard setting bodies such as the International Association of Insurance Supervisors (IAIS) display the rising political relevance of protecting financial service consumers. Several important **principle documents** have been developed related to financial or (micro)insurance consumer protection, including the OECD High Level Principles on Financial Consumer Protection and the SMART Campaigns Consumer Protection Principles (refer to Annex 2). The IAIS Insurance Core Principles and Guidance also include provisions related both directly and indirectly to consumer protection.

Concrete **implementation support from global actors** to carry out consumer protection work at industry level appears at this time to be limited to the SMART Campaign with an implementation tool for microfinance institutions that also includes comments from the MIN CP Task Force and Performance Indicator Working Group. At the policy and regulatory level, some broad guidance is available, including the IAIS Application Paper on Inclusive Insurance Markets and the CGAP Guidance on Regulation and Supervision in Microfinance.

At the national level, policymakers, regulators and insurance supervisors[3] have in some countries started to enhance consumer protection by introducing microinsurance regulations, specific complaints systems or financial literacy programs. Still, in most countries consumer protection regimes do not focus on low-income clients, microinsurance products and their providers. Policymakers and supervisors increasingly recognize that microinsurance requires special attention to secure consumers' rights and promote sound market development.

On the private sector side, there are attempts by some insurers and intermediaries to respond to the consumer protection challenge. Insurers make products simpler, sell and service them in many often non-traditional ways. Insurance or microfinance associations introduce codes of conduct and train the industry.

In sum, a variety of stakeholders have started to develop protection measures for microinsurance consumers. A holistic[4] **view of consumer protection in microinsurance that draws on the first experiences around good practices** as presented in the following can serve as a point of reference for authorities and the industry.

3 In this document, the term »supervisor« is used for the insurance supervisor who often plays both regulatory (rule creation) and supervisory (rule enforcement) roles.

4 »Holistic« means that the view considers all actors at the three levels: micro = client and provider (insurer and intermediary); meso = service providers (associations, training institutes); and macro = authorities (regulation, supervision, policy).

3 Protecting the consumer – a holistic view

In order to develop good practices based on a holistic view of consumer protection in microinsurance, this section starts by structuring the insurance process from a consumer's perspective in **seven steps**:

(1) As a precondition to becoming insured, a consumer would ideally identify and prioritize the risks he faces and obtain information to decide whether microinsurance is an adequate and affordable **risk-management option**.

(2) He then chooses a specific **product**

(3) from a suitable **provider**

(4) before eventually **purchasing the insurance product**.

(5) The consumer has to **maintain and renew a policy** if a policy period ends,

(6) **make a claim** in case the insured event occurs and

(7) be able to file a **complaint** and get redress if something in the process goes wrong.

Along these seven steps, a number of preconditions need to be fulfilled to ensure that a policy-holder can take full advantage of the insurance coverage:

Microinsurance consumers should be able »to make informed judgments and to take effective decisions«.[5] This requires them to be financially literate, i.e. to know and understand the concept of insurance as a risk management option, and to understand how to access the relevant information on products and providers. Consumers also need to know what their responsibilities are, what options they have in the event of a claim and in the case of a dispute. If the consumer is informed about these factors and understands them, he is able to protect himself from inappropriate products or sales techniques and can enforce his rights as a policyholder in all the steps of the insurance process.

In the ideal case, **insurance providers** (i.e. insurers and intermediaries) offer appropriate and valuable risk management products and adhere to the promises of cover and service they make through those products. In the ideal case, they also ensure that consumers have access to the information and services they require in order to understand those products and to use them effectively.[6] The insurer is responsible for managing risk effectively and in a financially sustainable way, and the intermediary for delivering the product in a manner that is efficient, honest and transparent. Both may be responsible for processing and administering claims in accordance with the promises made to clients and both are responsible for acting in a straightforward and transparent manner toward consumers at all times.

5 Definition of financial literacy according to UK National Foundation for Education Research.

6 It is important to note that this obligation typically does not extend to providing advice to clients on which products they should buy and how much coverage they need. Some providers are in fact legally prohibited from giving advice on microinsurance products, as in the case of South Africa.

Figure 1: The seven steps of the insurance process

Policymakers, regulators and supervisors should create a conducive policy and regulatory environment, including proper enforcement. The insurance supervisor is the keeper of last resort, and as such, the agency in charge of protecting the consumer. Supervisors need to control providers' operations to make sure they operate on a sustainable basis and are able to keep their commitments to the consumer. Regulations should further motivate providers to offer valuable products and services in a fair and transparent manner, including disclosure of product information, provision of necessary policy documents and establishment of effective and accessible complaints mechanisms. Regulation can create incentives to enter the microinsurance market by doing away with regulatory barriers that unnecessarily add to the cost or other burden of offering microinsurance and related services. Such a regulatory environment can create market conditions that provide the low-income consumer with confidence in the products they purchase and the providers that sell them, thereby promoting sustainable consumption.

In the Consumer Protection Guidebook Microfinance from the Philippines (2007) consumer protection is defined as »[...] measures that promote the rights of clients, enable them to make informed choices and protect them from unscrupulous acts that deny them the true value and optimum benefits of microfinance services such as credit, deposits/savings, insurance, and remittances and transfers«.

The table below summarizes an ideal insurance process and suggests what insurers and supervisors might contribute to such an ideal state. In real terms, there are conditions that impede such an optimal situation. The following two sections look at challenges in implementing a consumer protection agenda related to industry stakeholders, regulators and supervisors, and highlight some effective approaches and best practices to consumer protection.

Box 2: What can happen to an uninformed consumer?

Central to an effective consumer protection regime is the requirement that consumers be adequately informed about the products available to them. Uninformed insurance consumers are l**eft vulnerable to wrong choices and deceptive sales** practices. Some may purchase insurance even though another option such as savings might be a better option. Or, a policyholder may purchase insurance believing that she will get something back even if the risk event does not occur, confusing insurance with a loan, savings, or other financial service she may know. When mandatory life insurance is bundled with a loan, the consumers may not even know that they have insurance. Or, they may not understand what risk and which situations are covered, how much they will receive when they make a claim or the process to collect claims. Consumer's lack of knowledge and experience may also mean that they may easily bend to sales pressure. They may act on unreliable information from friends or family, or be pressured by a provider into purchasing insurance rather than truly understanding the product and making a conscious, informed choice.

Their lack of understanding **affects their ability to exercise rights** before but also after purchasing an insurance product. They may be unaware of rights such as the option to step back from a contract (e.g. cooling off periods during which they may be able to cancel a signed policy). They may not know where and how to seek redress or lack confidence to defend their rights, either because this information was not provided to them or because they did not understand the language and/or wording used in the policy or by the agent. Finally, they may not understand their duties and responsibilities under the insurance policy (e.g. paying premiums in time or informing the insurer about changes in their personal situation).

The combination of these factors **creates increased vulnerability, confusion, and intimidation**, which may lead to no purchase at all, a sub-optimal choice of products and providers, a purchase decision that the consumer does not dare to or cannot revert or a consumer becoming victim of misselling or fraud by a provider.

1 Information

Step 1	Consumers should be able to ...	This suggests that ... providers ...	supervisors ...
Obtain information about risks and risk management options	... collect and process information about the risks they face and the different options they have to cope with those risks. They should: • Generally understand the likelihood of a risk event and the expected cost if it materializes. • Know where to go to collect the information needed to make an informed decision and to get unbiased assistance in evaluating options. • Be capable of prioritizing the risks that are most important to cover with insurance. • Be able to decide whether microinsurance is an appropriate instrument or whether tools other than insurance (such as savings or emergency loans) are better to cope with the risk.	... inform clients transparently about insurance services ... ... and: • Provide detailed and unbiased information about microinsurance products in a way that low-income, often illiterate, clients understand. • Participate in efforts by regulators, insurance associations and others to educate clients and potential clients about microinsurance as a risk-management tool.	... promote financial literacy and ensure that appropriate information is available to consumers. This includes to: • Promote and facilitate education of low-income consumers about risk-management strategies, including microinsurance as one option to manage certain risks. Ideally, these efforts should be part of a wider financial literacy strategy at national level. • Ensure transparency of information that is accessible to the target market regarding e.g. clear publication of product characteristics, conditions and prices. • Ensure providers disclose information on a product in a simple and standardized form that allows comparison across providers.
CP aim:	**Consumers have the information and financial capability needed to make an informed choice about whether to purchase insurance.**		

2 Product

Step 2	Consumers should be able to ...	This suggests that ...	
		providers ...	**supervisors ...**
Choose a product	... use their understanding of risks and microinsurance policies to select the most appropriate product for their needs. They should: • Be aware of available microinsurance products and understand how they work. • Obtain complete and understandable information about the different products' terms and conditions, including price and payment structures, quality, benefits, limitations and exclusions. • Be able to decide whether the benefit(s) promised are attractive (or meet their needs) and affordable in the long run.	... design viable and appropriate microinsurance products ... ... and: • Develop and offer viable products that have clear value for the target market. • Create appropriate and simple product features and processes to ensure products are easy to buy and manage. • Gather risk data from non-traditional sources[8] and track client experiences over time to yield more appropriate pricing and product design. • Develop products and processes that reflect the limited risk microinsurance products pose to insurers. This will often require few to no exclusions within the range of covered risks. • Track performance of each product to have early information on products viability.	... ensure that insurance products reflect consumers' needs and abilities and are viable. This includes to: • Ensure that basic facts of a product (price, terms and conditions, commission) are disclosed in a transparent, timely and understandable manner by insurance providers (e.g. through standard information disclosure or a master policy document to allow easy product comparison), while avoiding an overflow of information. • To the extent appropriate, require simple products with few to no exclusions. • Do not discourage product innovation through excessive regulation. • Require the industry to report on key performance indicators to monitor financial viability and the client value of respective products.
CP aim:	**Consumers have access to and the ability to choose understandable, affordable and valuable products.**		

7 Non-traditional sources of information could be: neighbourhood representatives, financial institution records, specific hospitals that treat primarily low income patients, government statistics offices, and others. Many countries have some information on mortality and morbidity but it is typically challenging to locate and requires creativity.

3 Provider

Step 3	Consumers should be able to ...	This suggests that ...	
		providers ...	**supervisors ...**
Choose a provider	... choose the best provider (and its agent, intermediary or point of sale) among several options for their needs without being pressured into an inappropriate selection. They should: • Be aware of choices between different providers even if that means shifting to another linked relationships such as borrowing. • Understand the potential shortcomings and advantages related to different types of providers. • Be able to access the different options and have criteria to compare those options to select a trustworthy provider.	... be financially strong and manage their product distribution well ... ... and: • Ensure that all products they offer are monitored and at least show a trend towards profitability in a reasonable time. • Make every effort to reduce administrative and operational costs so products are efficient and affordable for the market they serve. Track the expense ratio. • Oversee the microinsurance operations of their intermediary partners to ensure value is conveyed to clients. • Set appropriate incentives for intermediary partners/sales agents to avoid deceptive sales practices.	... ensure that providers are financially strong and committed to providing value to the low income market. This includes to: • Ensure all insurers and intermediaries are effectively regulated, which requires licensing and supervision of informal providers. • Ensure that regulation is proportionate, i. e. appropriate to the nature, scale and complexity of individual insurers and their products, e. g. adjust the licensing/registration of microinsurance products and intermediaries. • Ensure the solvency of insurers without posing excessive compliance burden that may make it unviable to serve the low-income market. • Facilitate capacity-building of providers and intermediaries through more flexible requirements than in general insurance markets. • Hold insurers responsible for provision of services by their intermediaries.
CP aim:	**Trustworthy and financially sound providers and additional protection in the event an insurer suffers a financial collapse.**		

4 Purchase

Step 4	**Consumers should be able to …**	**This suggests that …**	
		providers …	**supervisors …**
Purchase the policy	… easily navigate the process of purchasing and paying for it. They should: • Be able to easily navigate paperwork. • Have access to clear and simple payment procedures. • Understand the terms and conditions of the product. • Understand their rights to refuse to buy a product, especially one tied to another product or service such as a loan.	… ensure that sales processes and policy documentation are fair, transparent and yet simple to reflect only necessary information … … and: • Ensure that marketing and sales practices are transparent and do not mislead clients, and that coverage is clearly and consistently explained. • Provide information, also for mandatory or bundled products, to ensure clients understand the policy terms and when and how to make a claim. • Use policy documents that are simple, clear and suited to clients' level of education and sophistication. • Group policies do not have to be individualized but a client should at least have a document that notes coverage, claims procedures, and complaints procedures.	... create and enforce rules to avoid deceptive and misleading marketing and sales practices. This includes to: • Prohibit aggressive sales, e.g. by requiring the provision of withdrawal periods (cooling off periods). • Require a (non-individualized) policy document to be handed to the consumer at the point of sale that provides contract details in a concise and understandable form. • Require that a policy be considered active from the payment of the first premium to the agent. • Ensure that client data is protected. • Publish ratings
CP aim:	**Sales processes that are appropriate and accessible for microinsurance consumers, allowing them to make informed purchase decisions**		

5 Maintain

Step 5	Consumers should be able to …	This suggests that … providers …	supervisors …
Maintain and renew policy	… understand what is required to maintain coverage and renew the policy. They should: • Know the procedures required to maintain and/or renew the policy. • Understand how to cancel a policy if desired in case it automatically renews. • Understand the payment structure and make required payments. • Know what happens if premium payments are not made or delayed in case a risk event occurs, or if other requirements are not met.	… create payment mechanisms that are clear and facilitate payments by people with low and sometimes irregular in-comes … … and: • Create premium payment processes that are transparent and clearly communicated to clients. • Create payment structures that respond to clients' abilities and penalties for non-compliance that are fair. • Employ straightforward and accessible procedures to maintain and renew policies, and clearly communicate those terms and conditions to clients. • Communicate any automatic renewal or any changes in coverage clearly to clients. Clients should be able to make decisions about con-tinuing when policy terms are adjusted. • Track the renewal rate and act quickly upon low rates, to identify and react to the reason, such as weak product design, communication or lack of adequacy of products or processes for the client.	… ensure conditions under which continuity of cover is made clear and easy for the low-income client. This includes to: • Ensure that terms and con-ditions to maintain and renew policies are clear, simple, and timely communicated to clients. • Require providers to clearly and timely inform about premium payment processes. • Facilitate innovative premium payment options by coordi-nating with respective regu-latory bodies, such as Central Banks or Regulators of Mobile Technologies. • Enable payment mechanisms that are adequate for people with low and irregular inco-mes. • Require any automatic re-newal and any changes in coverage to be clearly com-municated to clients in a timely manner. Clients should be able to make decisions about continuing when policy terms are adjusted. • Track client experiences by commissioning consumer research and adapt regulatory requirements as appropriate, e.g. by requiring the publica-tion of renewal rates.
CP aim:	**Appropriate and transparent payment and renewal procedures and adequate after-sales customer care**		

6 Claim

Step 6	Consumers should be able to …	This suggests that …	
		providers …	supervisors …
Make a claim if an insured event occurs	… understand what is covered and what the requirements are for making a claim. They should: • Understand (know and re-member) what is covered and what is not. • Be aware of the process for filing a claim (where and how) and understand with the requirements. • Be able to provide the simp-lest possible documentation that clearly confirms the occurrence of the covered event without unnecessary time or monetary investments. • Track the promptness of claims settlement and claim rejection ratio, and limit delays (e.g. onerous claims requirements).	… create clear, easy-to-follow and timely procedures for ma-king claims and process claims as promised … … and: • Provide claims applications that are easily accessible and simple to complete. • Use documentation require-ments that are no more onerous than necessary to prevent fraud and result from a risk-based approach. • Settle claims as rapidly and efficiently as feasible and adhere to conditions laid out in the policy. • Use policies that help facili-tate simple and efficient claims settlement and rapid disbursements. • Track the promptness of claims settlement and claim rejection ratio, and limit de-lays (e.g. onerous claims requirements).	… ensure that effective claims processes are in place. This includes to: • Monitor whether claims processes are in line with the insurer's stated policy and handled in an efficient way. A maximum settlement period might be set. • Ensure that claims application is easily accessible and simple to complete. • Allow documentation re-quirements for claims that are no more onerous than neces sary to prevent fraud; ideally in a standard and concise form. • Enforce effective and fair claims management by requiring insurance providers to monitor their claims per formance, including the claims ratio, timeliness of settling and disbursing claims.
CP aim:	**Claims processing that is straightforward and prompt**		

7 Complaint

Step 7	Consumers should be able to …	This suggests that …	
		providers …	supervisors …
File a complaint if something goes wrong	… seek and obtain redress if something goes wrong. They should: • Be aware of the option to file a complaint and know how to do it. • Be able to rely on a process that is understandable, can be navigated easily and has no high transaction costs. • Be able to rely on a process that is understandable, can be navigated easily and has no high transaction costs. • If the complaint is not resolved at the first level (e.g. insurers service desk) be able to escalate it to a higher level (e.g. ombudsman).	… create an accessible and effective mechanism for complaint lodging and resolution … … and: • Maintain an easy-to-use complaint resolution policy and processes that allow quick solutions. • Employ systems for tracking all complaints and their resolutions. • Track complaints ratios and act upon signals. • Make efforts to facilitate the resolution of client problems and issues before they raise to the level of formal complaint. Provide incentives for intermediaries to act upon this premise. • Include microinsurance-related issues in the company's feedback mechanisms	… make sure that effective, independent and accessible complaints mechanisms exist. This includes to: • Require insurance policies to clearly state how to file complaints. • Require insurers to create an accessible and effective complaint mechanism, for example, by offering the possibility to file complaints via innovative channels (e.g. mobile phone, community leaders). • Foster training and accreditation of dispute mediators that can deal with this client segment. • Require the industry to fund and appoint an independent third party such as an ombudsman (or dispute resolution mediator) to handle com plaints that could not be resolved by the insurer in first instance. • Monitor the number of complaints of insurers and how they were dealt with. The supervisor should have access to the industry's complaint tracking system. A special view on microinsurance is necessary as low numbers may indicate that the service is not known or easily accessible.
CP aim:	**Accessible and effective complaints and redress options in the case of a conflict**		

4 Insurance industry - challenges and current approaches

Many of the most immediate consumer protection challenges, as well as efforts to protect consumers, occur at the industry level. This section begins by exploring the industry-level consumer protection challenges facing microinsurance consumers. We then discuss emerging efforts to address these challenges at the micro (provider) level, and go on to describe the supporting efforts of meso-level players.

4.1 Industry level consumer protection issues: insurers, intermediaries, products and administration

To set up a viable microinsurance business, it should be in the insurer's own interest to establish a good reputation, keep commitments and avoid over- or mis-selling of insurance products to achieve »quick wins«. Insurance is a business of trust, hence (potential) consumers will not buy a microinsurance product if they do not trust the provider, unless forced or misled. However, insurers and intermediaries face numerous challenges to build a sound microinsurance portfolio and must balance consumer protection concerns with the need for efficiency and with the many logistics constraints they face.

4.1.1 Formal and informal insurers

As microinsurance markets begin to mature, the number and variety of providers continue to increase rapidly, as they have over the past decade. This expansion has created tremendous benefits for clients as access has dramatically improved for many low-income families. The growing number and array of providers has increased competition, yielding improved pricing, design, variety and servicing of products to better respond to the needs of the target group. Advances in technology have added opportunities for efficiencies that are helping to reduce costs and facilitate efficient and effective servicing, as well as the potential to improve consumer protection.

The dynamism of the microinsurance industry has helped to improve consumer protection in some respects, but it also generates new challenges related to insurers and intermediaries. Each insurer type raises distinct consumer protection concerns:

Commercial insurers bring risk management skills as well as capitalization and access to reinsurance. However, they often have limited understanding of low-income consumers. The tendency to apply their knowledge of traditional insurance and related skills to microinsurance often leads to mistakes that create problems for low-income policyholders. For example, marketing in the traditional manner is seldom effective in getting low-income, often illiterate consumers to understand, trust, and purchase a product. Traditional pricing models are limited due to the lack of quantitative risk data for the low-income markets leading to sometimes excessive loading of premiums and very low claims ratios. The traditional risk management strategies and controls of traditional insurance are often predicated on lists of exclusions and processes that have evolved for high-value policies. Their use in microinsurance opens much potential for confusion, overpricing, and rejection of claims that clients thought were covered. At the same time, the risk management needs that those controls respond to are typically much lower for microinsurance than traditional insurance.

Commercial insurers, who are most likely to drive microinsurance expansion, are responsible to shareholders for generating profits. Entering the microinsurance market with its challenges is a testament to their belief that microinsurance can generate corporate benefits in the long term.

The long-term sustainability of microinsurance for commercial insurers, however, depends on finding effective solutions to the consumer protection challenges they face.

Mutual insurers often bring insurance skills through professional management as well as experience with and understanding of the low income market. This is particularly true for the larger mutuals. They tend to be directly focused on products and processes that are effective for the low-income market and in protecting the rights of microinsurance policyholders. Their governance structure, which involves members, can help to maintain this focus where it is effective. However, these member-constituted boards often have limited capacity. Mutuals are certainly not immune from consumer protection issues simply because they are member owned.

Informal insurance providers such as unregulated community-based programs are close to clients as they are typically geographically close to them as well as member-managed and governed. However, these providers tend to be weak organizations that struggle to uphold their promises, and their small size and location in often remote areas can pose a prudential risk. The limited skills of management and boards can create significant potential for consumer protection problems. For example, limited risk management skills can lead to under-pricing and over-promising, which can leave legitimate claimants without cover. These groups usually operate outside the purview of financial supervisors. Even if a group is licensed and supervised by a non-financial authority, that authority often lacks the skills and resources to conduct effective supervision of insurance activities. Limited oversight can also exacerbate or even create a conflict of interest, as when the supervisor is also a promoting agency.

Weak supervision coupled with weak governance opens the potential for significant mismanagement and fraud, and ultimately many opportunities for consumer protection pitfalls.

Informal service providers such as funeral parlors are common in some countries and sometimes offer insurance products. These service providers may have a clear understanding of the risks their customers face and the related costs, but they often lack appropriate knowledge, incentives and external controls to protect clients' interests, leading in some cases to fraud or inability to cover claims. They also face the prudential, oversight and risk management challenges as informal insurance providers.

4.1.2 Intermediaries[8]

In microinsurance, the variety of intermediaries is greater than in traditional insurance. Low-income people need to trust the person or organization that sells them the insurance, and they may not trust traditional insurance agents. In the traditional market, it is relatively easy to structure consumer protection policies around an easily identifiable group of licensed agents. Microinsurance makes this much more difficult and opens concerns on several levels of the sales and customer service processes.

In order to increase access to microinsurance, it has become clear that policies need to be sold through **non-traditional intermediaries**. Options for intermediation continue to grow with the increasing involvement of church groups, electricity companies, retailers, telecoms and others.

In microinsurance, **agents** are especially important in helping the insurer access the low-income market. Over time, the role of agents in microinsurance has significantly expanded from simply selling the product, to helping insurers with product design, marketing, servicing, claims processing and adjustment. At the same time, the individuals who actually sell the products (for example, microfinance institution field staff, retail clerks, union leaders and cell phone airtime dealers) are often unlicensed, untrained and lack knowledge of insurance. They often have another primary activity (such as selling another service or product) and microinsurance sales are added to their responsibilities. Agents who sell microinsurance play a more important and more extensive role than traditional agents, but often have less training and knowledge, are subject to less oversight, and therefore create greater potential for fraud and mis-selling. These dangers, while significant, must be weighed against the need for an effective channel to reach microinsurance clients.

Microinsurance **brokers** have been active in some markets. Typically they work between the insurer and an institutional agent such as an MFI, adding a layer of administration but also often taking on a substantial back office role in insurance intermediation, product development, marketing and training activities. This leaves both insurer and institutional agent with more limited roles.

Microinsurance focused sales forces are also commonly found. However, they are often inadequately trained in insurance and subject to high turnover. As a result they often fail to give consumers accurate or complete information.

The **long value chain** created by microinsurance intermediation, while needed to reach many low-income consumers, can lead to conflicting motivations. Agent commissions tied to microinsurance sales can create incentives to make decisions that go against the best interests of clients. For example, the conflicting interest of the institutional agent can arise when it wants to both improve their own profitability and sell valuable products to their clients. Although a balance between value and profitability is certainly possible, it is often hard to achieve. Often, those who should advocate for clients focus too

8 Traditional insurance typically accesses policyholders through intermediaries. These delivery channels or intermediaries include agents that are licensed to offer the products of one insurer they represent, and brokers, that are licensed to offer products of any insurer, since they represent clients, not insurers. Both parties can have an important role as the interface between the insurer and the consumer. Sales forces are insurers' own sales staff.

much on their own profitability, selling to consumers products that may provide more value to themselves than to the consumer (for instance, products with coverage that does not reflect the needs of clients but brings high commissions). At the same time, in the absence of substantial commissions or other financial incentives, most intermediaries would lack the motive to focus adequately (if at all) on microinsurance, limiting the outreach of these products.

Intermediation may also make **accountability more difficult**; employees or agents acting fraudulently or misappropriating premiums or claims are less likely to be discovered and held accountable as the total number of parties involved increases. Low-income people are particularly vulnerable in this respect, as they are often less able and/or likely to successfully challenge unfair treatment. However, different parties are also responsible and may watch for each other's actions, to some extent.

4.1.3 Product-related issues

Offering products that protect clients – through transparency, honoring the commitments, and prioritizing simplicity and clarity in the design of products and processes – helps clients to experience insurance in a fair and proper manner. This is a vision which is not always in line with common practice. In the following section, we identify some of the challenges related to products currently being offered to the low-income segment.

A significant proportion of typical coverage in microinsurance is **credit-linked life insurance**. Institutions that offer such compulsory or automatic insurance, mainly as credit-life products linked to microcredit, do not have pressure to »sell« the products. These compulsory products are also easier to overprice, when in fact such simple products sold automatically to clients typically should be relatively cheap. Furthermore, clients are often unaware that they have insurance. Even if they are aware

Box 3: Product features that make consumer protection easier

Low-income consumers require **rapid claims** settlement. This requirement has led to changes in both product design and claims processes. Low-income people relying on a basic term life benefit to bury a family member cannot wait months for their USD 500 claim to be settled. Ninety days could be a long delay if the consumer was led to believe that the money would be available immediately to cover burial expenses. This timeframe is a potentially serious consumer protection problem with respect to a microinsurance policy, while it can be easily acceptable and fair for a USD 500,000 policy held by a wealthier policyholder. This is particularly true in light of the fact that a high-income consumer generally has greater access to other risk mitigation tools (such as savings or loans) that can be used to bridge the gap while waiting for the insurance benefit.

To allow faster claims payments, the insurance policy must be simple and should require less documentation to confirm that the insured event (e.g., a covered death) has in fact occurred. It is typically most appropriate to have a simple contract defining **few if any exclusions**. This reduces the time required for the claims process, since it is only activated to confirm the event occurred and that the few exclusions did not occur. It also makes it easier to explain to clients what the policy does and does not cover, improving the environment for consumer protection. Indeed some microinsurers offering term life policies simply say, »if the client dies we will pay …«

they have a credit life policy, the product is still too often designed with a focus to protect the lender more than the client himself. Borrowers typically have no ability to select the insurance provider and there is little transparency regarding pricing. Since borrowers are often compelled to purchase the insurance product in order to access the loan, they often have limited capacity to challenge the conditions. Such a structure is ripe for inadequate products and unfair pricing.

Health insurance is often complicated and ensuring that clients have clear information about the product's coverage and how to make claims can be a challenge, even in traditional markets and particularly in microinsurance. The involvement of the health care provider increases the potential consumer protection issues. Providers may offer different care to those with microinsurance coverage and may prescribe unnecessary treatments that add costs resulting in higher premiums. They also add a layer of complexity to the process of using insurance, increasing the chances of a mistake or misunderstanding.

Products that present a real or perceived risk of client fraud (such as **accidental death insurance**) can have complicated and onerous documentation requirements that are difficult for low-income consumers to understand and meet and erode the product value by adding significant costs. At the same time, these products may in fact create a real incentive for consumers to commit fraud. For example if accidental death pays more than natural death, beneficiaries may have incentive to make it appear that the death was an accident.

More **complex life insurance** products, such as those that cover family members, can also require burdensome documentation to file a claim. Low-income people, especially in rural areas, may commonly lack required documentation such as birth certificates to prove the relationship between the deceased and the policyholder. Such complex life products are often linked to a savings component (such as an endowment). The savings component opens the door to a number of consumer protection issues, including:

- ambiguous promises of a long-term return on savings;
- strict lapse policies on the insurance policy that can result in loss of savings;
- conditions on lending from the long-term savings which include high fees and interest rates;
- risk to the long-term viability of the insurer itself; and
- macroeconomic issues such as hyperinflation that can wipe out policyholder savings.

Index insurance to address catastrophic agricultural events is designed to be transparent and to provide prompt claims settlements by eliminating documentation requirements. However, basis risk (the risk that the payment the consumer receives does not match the value of the loss that he suffered) of these policies is often significant. A consumer may lose an entire crop without reaching the index trigger, and therefore not be entitled to coverage. Often, these products are difficult to understand and explain, leading to the risk that consumers are insured but without proper understanding of the coverage, how it works, or what it is worth.

4.2 Industry practices to improve consumer protection

The issues mentioned above present significant, but not insurmountable challenges to consumer protection in microinsurance. The experiences of various industry stakeholders have begun to reveal lessons about how industry players can work to meet consumer protection needs.

4.2.1 Micro-level consumer protection efforts by providers (insurers and intermediaries)

Building a relationship of trust with their clients by providing valuable products that clients understand, adhering to commitments and by operating profitably through appropriate processes and business models, should be in the insurance company's own interest to reach long-term viability. Further, in the ideal case, the insurance company will have the incentives and capacity to pressure intermediaries and others who act on its behalf to meet consumer protection needs as well. As discussed in the previous sections, this ideal case is challenged by a number of particular issues relating to the nature of microinsurance business, type of providers and distribution channels, product design and incentives at play.

Processes and policies: While insurers need safeguards to protect against fraud and other risks they face, it is also important to honor commitments and avoid creating needless roadblocks to purchase and use of these products, which may exacerbate the vulnerable position of their low-income policyholders. Improving processes and policies to make them appropriate for the size and type of the insurance policies and the needs and characteristics of the consumer improves the environment for microinsurance and goes a long way to improving consumer protection. Insurers and intermediaries need to develop risk-based business practices for microinsurance products, considering consumer protection throughout the business process and the consumer's interactions with them. Such an approach requires careful attention to different parties' roles and responsibilities, incentives, staff and agent training, infrastructure and processes that can address potential concerns.

An important part of consumer protection is making sure that the insurer manages processes and controls in an effective and viable way that is proportionate to the nature, size and complexity of the policy, for example:

- Tracking key performance indicators[9] and reviewing those indicators based on targets set by the intermediary and insurer with a conscious effort to target results that protect clients.
- Developing a risk-based approach to documentation requirements and other controls. With small-value policies, controls should reflect the limited risk through reduced and appropriate control strategies. This may require training and international guidance.

Sales: An important part of consumer protection is ensuring that products are sold responsibly. This includes developing mechanisms to hold insurers responsible for the sales practices and other actions of intermediaries acting on their behalf (especially when those intermediaries are unlicensed or operate under limited licenses that call for insurer oversight). This responsibility includes:

- Testing (through regular focus groups, client interviews, or some other means) new marketing materials, marketing strategies, enrollment procedures and documentation with potential clients to ensure proper understanding even for automatic or mandatory products.
- Reviewing compensation strategies and the incentives they create to mitigate the potential that products will be mis-sold by agents.
- Linking agents' compensation to the actual costs they face to deliver and service products plus a fair profit margin.

Products: Providers of microinsurance have recognized a number of **product characteristics** that set this market apart from traditional insurance. Among these differences is the need for:

- rapid claims settlement;
- very simple products;
- use of a wide range of non-traditional »agents«, some of which may not be subject to traditional licensing;
- limited and simplified paperwork requirement and processes; and
- alternative approaches to insurance controls and risk management measures.

Staff Training: Particularly in the case of non-traditional and/or unlicensed delivery channels, staff may lack understanding of basic concepts of insurance, how to explain insurance to clients, and relevant ethical considerations. Training staff in terms of this often entirely new type of business and client segment can refer to, for example:

- training on basic concepts of insurance, when it is appropriate, and how it works;
- information on details of the products they sell, including any requirements, exclusions, or limitations and the processes needed to enroll and maintain policies and to file claims;
- ethics training to communicate to staff what potential consumer protection concerns are and what they are expected to do to minimize those concerns; and
- adequate sales force training that ensures sales personnel understand the clients and products and can communicate effectively with these clients

9 For more information on Financial and Social Key Performance Indicators, please visit the Microinsurance Network's Performance Indicators Working Group's Website: *http://www.microinsurancenetwork.org/workinggroup/Performance/9.php*

4.2.2 Consumer protection efforts by meso-level institutions

To protect consumers from intentional or unintentional mis-selling and unfair or unviable insurance practices, the industry needs to be regulated and supervised and have support structures available that help to improve capacities. Especially in countries with weak regulations and insurance supervisors with low capacity, meso-level actors and other support institutions such as associations, training institutes and other civil society bodies can play an important complementary role in promoting self-regulatory approaches and build supportive infrastructure for protecting consumers more effectively (see Box 4). They can support insurers in the following areas:

- provide training for product development, sales and ethics;
- facilitate the development and implementation of a code of ethics and find effective ways to monitor/enforce it;
- implement and facilitate literacy work at the intersection of industry and policy;
- motivate the industry to establish accessible complaints mechanisms such as an ombuds-

Box 4: Meso-level actors supporting the consumer protection agenda of their members

- Industry associations such as FASECOLDA in Colombia represent their members and can push a network-wide or even national consumer protection agenda for improved capacities and systems. They also help to set collective standards for consumer protection, communicate common problems and solutions to members, and provide valuable information to consumers. Some associations (e.g. actuaries' associations) can also address data requirements and help in increasing the understanding of the components and quantification of risk of the low-income market. Others can be helpful in generating and disseminating public goods like market studies and codes of conduct for microinsurance, as well as ethical market education. A code of conduct can introduce a self-regulation mechanism including peer review. Associations can also monitor sector performance while emphasizing the ratios that are most relevant to consumer protection (claims ratio, renewal ratio, surrender value and claims duration, for example).

- Training institutes can develop and implement training sessions for managers or sales staff, such as the course by the Rural Bankers Association in the Philippines. They create curricula and training materials that are used by providers and others to conduct training within their institutions. Training institutes can focus on: (a) developing products and processes for the low-income market; (b) developing standard pre-approved policies making them as simple as possible; (c) developing and implementing appropriate sales strategies for microinsurance; and (d) providing ethics training in various topics.

- Dedicated civil society bodies such as consumer protection agencies can be helpful in developing policies to complement the work of industry associations and in monitoring implementation. They can integrate financial services into their work and link up with the financial and/or insurance sector while sharing lessons from consumer protection efforts in other industries.

man, and secure funding for this mechanism; and

- support the industry dialogue to provide inputs to develop appropriate regulations, advocate for regulatory changes and include industry perspectives in discussions of such matters.

The implementation of consumer protection strategies can be achieved by meso-level actors at operational and at policy levels. At the operational level, they can introduce and enforce codes of conduct, offer training for staff of insurers and intermediaries, and ensure the quality of loss adjusters and actuaries. In cooperation with policymakers, central banks and insurance supervisors, they can help implement financial literacy efforts such as public-private campaigns or national strategies. They can also support public-private dialogue and lobby for regulatory changes (see Section 5).

Support institutions can facilitate the development, implementation, and monitoring of a better consumer protection environment. In most countries, which have limited or no microinsurance-specific consumer protection policies, regulations or efforts, this should be focused on insurance in general, with components that are specific to microinsurance. The implementation of consumer protection mechanisms is predominantly a private sector task, and support institutions play an important role, but one that requires clear rules and enforcement of those rules from the supervisors' side.

5 Policy level – challenges and current approaches

Effective consumer protection regulation in micro-insurance encourages the development of **market conditions** which provide low-income financial consumers with greater confidence in the products they purchase and the providers who offer those products, thereby promoting sustainable consumption. In recognition of the failures of markets, an increasing number of policymakers and insurance supervisors in emerging markets and developing economies have prioritized the protection of financial services consumers. We observe policy approaches such as the creation of a specialized consumer protection body, the promotion of financial literacy, or interagency coordination; and regulatory approaches such as creating a dedicated prudential or market conduct framework that focuses on the type of provider and product suitable for the low-income consumer.

5.1 Issues for insurance supervisors

Insurance supervisors often have **little knowledge or awareness** of the target client group for micro-insurance as they often lack reliable data to inform their work. They also often lack information about innovations in microinsurance (in products, processes, and regulation) that are happening in their jurisdiction, and effective microinsurance business and regulatory approaches of other countries.[10]

Supervisors are often challenged with **limited funds** to acquire, train and retain qualified staff, to develop innovative approaches to microinsurance regulation and supervision and **to build good control and information systems**. This creates a significant trade-off between maintaining the current situation that provides at least a level of certainty about the current supervisory role, and investing in advancing a new market that would require more supervisory capacity and funding and lead to greater uncertainty.

Supervisors **may lack legal protection to support their supervisory actions and decisions**, which may lead to lenience or forbearance, perpetuating undesirable market practices. With such conditions, supervisors are ill-equipped to implement the regulatory and supervisory reforms and improve their internal capacity; they often lag far behind providers and market innovations.

In addition, **complaints mechanisms** are often non-existent or ill-suited to the low-income segment. This increases the burden of supervisors, who as a result often become consumers' first resource when a problem occurs.

In most countries, the existing insurance regulation was **originally created with higher income clients and traditional (higher-premium and higher-benefit) products in mind**, which is also the case for consumer protection laws and regulations that apply to financial services more generally. Adapting practices to the reality of low-income consumers and the different offerings targeting this group is another challenge faced by supervisors today. They need a clear vision and strategy that aims at understanding the needs of low-income consumers and enhancing their ability to access and effectively use microinsurance.

An additional complicating factor is the **cost of supervisory compliance** imposed on microinsurance providers and other regulated financial firms. With scarce financial and human resources support from the government side and the need to deal with low

10 The IAIS has contributed substantially to the development of a framework for consumer protection regulation for conventional insurance. With the adoption of the Application Paper on the Regulation and Supervision of Inclusive Insurance Markets important directions were provided for microinsurance.

margins from the provider side, cost considerations become even more important. Microinsurance contracts are very small and the business requires large scale to be financially sustainable due to narrow profit margins on individual policies. Supervisory cost can easily become a significant burden and make microinsurance unattractive to insurers or too costly for low-income families.

Consumers remain inadequately protected when regulation severely limits their access to insurance or leads to unnecessary costs. Hence, regulators and supervisors need to strike a delicate balance between promoting innovation and the growth of a safe microinsurance market, avoiding unnecessary harm to the business case for providers, while making the best use of scarce regulatory and supervisory resources.

5.2 Current policy approaches

Some jurisdictions created **specialized consumer protection bodies** to be responsible for developing and implementing policies to encourage good market conduct standards and safeguard the rights of financial consumers. Others have focused on their prudential oversight, making clear the link between consumer protection and systemic stability, a position that is becoming increasingly widespread. We know, however, very little about the extent to which microinsurance is integrated in these bodies, since it is a new market segment in most countries, from both protection and prudential oversight standpoints. In some countries, the prudential regulator (e.g. Brazil) or the market conduct regulator (e.g. Mexico) has engaged in research and inter-agency dialogue to look into the specific issues of protecting the microinsured.

Box 5: Country examples of consumer education

- **Kenya:** Industry and authorities, supported by the DFID financed Financial Sector Deepening Trust, joined hands in a national program on consumer education.

- **Ghana:** The Ministry of Finance, in cooperation with the Bank of Ghana and several international development agencies (USAID, GIZ), adopted a Financial Literacy and Consumer Protection Strategy. The National Insurance Commission (NIC) is in cooperation with GIZ promoting microinsurance education through numerous channels.

- **Uganda:** The Bank of Uganda together with GIZ has issued financial consumer protection guidelines »Towards an Effective Framework for Financial Literacy and Financial Consumer Protection in Uganda« (2011).

- **The Philippines:** The Department of Finance, supported by GIZ, ADB and industry participants, has issued a »Road Map for Financial Literacy« (2011) and supports its implementation. A series of trainings on Microinsurance Advocacy and public seminars on Microinsurance have been successfully rolled out in all 16 regions across the country with the Insurance Commission and the Department of Finance leading the whole process.

Box 6: Authorities with a primary role in consumer protection

- The **national insurance supervisor**, as the lead agency, is responsible for designing, implementing, and enforcing prudential and market conduct regulations and for guiding policymaking.
- The **supervisory authority overseeing other financial institutions** such as banks, MFIs, and cooperatives that could intermediate microinsurance will also play a role. Its supervisory choices can influence the development of microinsurance (e.g. on issues such as electronically authorized transactions or distribution channels).
- The **Central Bank** is in charge of the large value and retail payment systems, whose rules will determine, for instance, the openness to innovation in the way microinsurance premiums and claims are paid or the way microinsurance products are marketed and sold.
- The **Ministry of Finance** (MOF), or other similar policymaking agency is in charge of promoting microfinance including insurance. In some cases, it includes a **specialized financial consumer protection agency or department**.
- A **general consumer protection agency** is usually embedded into the Ministry of Trade or other branch of the government such as the Ministry of Justice, and plays a primary role in designing and in some cases enforcing consumer protection rules affecting microinsurance.

Policymakers in an increasing number of countries consider **financial literacy** to be among the most pressing consumer protection issues. Effective protection builds on insurance literacy of the low-income segment, since it is believed to create capable and confident consumers and foster the growth of the microinsurance market. Against this background, authorities have been increasingly engaged in a variety of policy approaches to **support financial literacy work**. For instance, a leading agency such as the Central Bank or Ministry of Finance may set-up a financial literacy agenda to which other authorities subscribe or commit. Sometimes such initiatives are launched in cooperation with the Ministry of Education, development agencies, and the insurance industry in order to build consumer awareness and trust. Some countries take a public-private approach to strengthening financial consumer education, including insurance (Box 5).

A good degree of coordination and information sharing between agencies is required. However, in many countries coordination among the public entities, as well as between them and the private sector, is weak or non-existent. For example, when the insurance supervisor may be reluctant or unaccustomed to involving the Ministry of Finance or Central Bank in its activities, it may create a situation in which different agencies follow different and sometimes overlapping or even conflicting financial access and education agendas.

In some countries, the Ministry of Health has partnered with private sector and financial services players to promote financial inclusion among participants in social protection programs. For instance, some conditional cash transfer programs are exploring the use of microinsurance as tool to help families »graduate« out of the programs and achieve greater control over their financial lives.[11] Making these authorities aware of each other's efforts, coordinating initiatives and clarifying their respective roles, especially the role of the lead agency, is critical.

There is enormous need for inter-agency coordination among the variety of government authorities that are involved in consumer protection in microinsurance. Among the authorities we distinguish primary from secondary roles in regulatory, supervisory, and policymaking (Box 4).[12]

The most important agency is the insurance supervisory authority, which acts as a »quasi auditor« – a controller of last resort. Insurance supervisors exist to protect clients from mis-selling, over-selling, improper handling of claims and other market conduct failures. The supervisor also monitors the financial health of insurers, working indirectly to ensure that the industry maintains prudent levels of risk-taking and that insurers follow good corporate governance practices that protect their financial position and therefore their ability to fulfill obligations to consumers (including for payment of claims). The secondary authorities might also actively cooperate with the insurance industry and the supervisor or undertaking isolated initiatives to promote access to insurance among underserved populations.

11 Some examples are Bolsa Família in Brazil, Familias en Acción in Colombia, and Opportunidades in Mexico.

12 Authorities with a secondary role: The Ministry of Education is involved in financial literacy work that may affect the relationship of consumers with microinsurance products. The Ministry of Health (MOH) and/or Ministry of Social Protection develop services and strategies to improve the livelihood of low-income families through far reaching programs such as unconditional and conditional cash transfers, job creation and food security. Depending on the jurisdiction, other ministries, such as telecommunications (in the case of mobile payments), food, women's affairs, small and medium enterprises, or agriculture may also play secondary roles. Tax authorities may play an important role in some countries, as differentiated tax regimes for microinsurance may be needed to facilitate the offering of affordable products to lower income clients.

5.3 Regulatory and supervisory approachesto consumer protection

An appropriate regulatory and supervisory framework, including efficient and effective supervision of providers, is key to ensuring consumer protection. Only when it exists can consumer confidence be built and maintained, grounded in the providers' good financial health and in fair products, processes, and treatment, as well as continued dedication and commitment to improvement of protection over time. The primary role of the insurance supervisor – like any other financial supervisor – is to ensure insurers' solvency and thereby indirectly protect consumers. To do so, supervisors concentrate on **prudential** requirements such as capital adequacy. However, many other issues are relevant such as regulatory standards for **market conduct, products or intermediaries and effective supervision**.

A – Prudential regulations include licensing requirements, capital adequacy ratios, minimum initial capital, liquidity, and operational standards. In this sense, prudential regulation and supervision protects an insured person against the insurer's insolvency and minimizes the potential losses when insolvency occurs. It also offers protection by ensuring common operating and internal control standards that minimize the risk of losses due to operational failures and frauds.

Informal providers such as funeral parlors, preneed services and small member-based schemes, assume an important social and economic function. However, they typically lack many prudential safeguards. Operations may fail due to inadequate corporate governance or risk management. Prudential regulation designed with large commercial insurers in mind is often too onerous for these small providers. As a result, small community-based mutuals may be unable or unwilling to register as formal insurers and become regulated entities. Creating a path for providers to formalize, perhaps through tiered prudential standards that better reflect the actual risks faced by different types of providers, can do more to protect those insured by informal

insurers than stringent requirements that those providers will never meet. Such an approach would allow regulators to create lighter prudential requirements for this sector, or even exempt them from prudential rules entirely while applying common market conduct standards.[13]

Operational standards may also have a profound impact on consumer protection. They include requirements relating to internal controls, internal audit and corporate governance that work together to avoid problems, failures and fraud that can severely impact consumers of a certain provider and sometimes even a whole sector. An example is the requirement for insurers to have systems to avoid, detect and deal with fraud, such as manipulation of a client's file. It is still unclear whether there are fraud issues specific to microinsurance.

A regulatory framework (including prudential and market conduct rules) that encourages and permits the **integration of informal players** who already work with low-income households into the mainstream insurance sector can encourage competition, innovation and greater protection. However, this must be done with care to ensure adequate supervision and enforcement and avoid undesirable providers. Supervisors in a number of countries have been considering to regulate informal insurance providers. The following are two examples of regulatory reforms to accommodate informal players, giving them a clear path to formalization:

- **South Africa's** Microinsurance Bill (2011) opens up a new type of license for microinsurers that will help informal providers to become licensed.
- The **Philippines** Supervisory Framework accommodates the new tier of »Microinsurance Mutual Benefit Associations« (2006). The revised Supervisory Framework (2010) allows a new category of »Microinsurance

13 An interesting example of this approach is found in the credit market in South Africa: all credit providers must be registered with the National Credit Regulator (NCR), but only larger providers are subject to prudential requirements, which are actually enforced by other supervisory agencies such as the South African Reserve Bank.

provider« (risk-carrier and brokers), with capital requirements that are half of those applicable to traditional insurers and brokers. It also includes a different training approach for microinsurance agents.

B – Market conduct regulation, which governs the distribution or intermediation of insurance products, aims to protect consumers (including low-income consumers) directly. These regulations include legal and regulatory minimum standards to safeguard consumers' rights regarding:

(1) Protection from practices that are unfair, deceptive, or abusive and from discrimination; including requiring proper advice and prohibiting some sales and collection practices.

(2) Disclosure of relevant, comprehensive, meaningful, comparable, understandable, reliable and timely information to consumers to help them make informed decisions[14], including requiring the use of standardized language and formulas to describe terms and conditions of an insurance policy.

14 In countries where many languages are spoken, the regulation usually require providers to create information, contractual and marketing materials in the main languages of the regions or places where the product is offered.

Information imbalances[15] between providers and consumers may be reduced with the introduction of minimum and common disclosure standards that are applicable across the industry. Supervisors may limit information disclosure requirements to key components to avoid consumers being overwhelmed by too much information. Supervisors may also require providers to clearly and under standably disclose information; this may include standardizing some terms that are used in marketing materials, insurance policies and other documents commonly handed to the consumer, with the purpose of ensuring comparability and easy understanding.

C – Product regulation: Simple and sometimes standardized product features make it easier for consumers to understand the insurance policy and procedures. Products with few or no exclusions or conditions are easier to understand, easier to sell (especially for informal »agents« who may be unfamiliar with insurance), particularly in a way that is not misleading. Claims are easier to manage for these simple products, from the perspective of the insured, insurer, and intermediaries. Product-

15 »At the heart of consumer protection are asymmetries of information between financial services product providers and the public to whom the products are sold« (IAIS ICPs).

Box 7: Reporting a claim can be costly

An insurance company in Peru offers a credit life policy to a low-income consumer that provides a benefit of USD 800. In order to make a claim on this policy, a beneficiary must provide a report of an autopsy and other examinations. These requirements ultimately cost about USD 300, and involve several months of waiting until the necessary documents can be secured. In the interim, beneficiaries borrow money from lenders at high interest rates to cover the costs of this documentation and to bridge the gap before receiving the insurance payout, further eroding the fund value received.

specific regulations can be particularly important for innovative index insurance products such a weather insurance. With payouts being linked to an independent trigger instead of actual experienced losses, these products are even more difficult clients to understand. This complexity, together with the problem of basis risk, greatly adds to the potential of misselling products to clients and/or lack of understanding of products.

Creation of a master policy regulation is sometimes considered a paternalistic approach but it may work well for microinsurance in most contexts. This type of regulation sets standard product features (or limits on product features) with the purpose of protecting consumers, recognizing that consumers do not always make the wisest decision even if they are well educated, financially literate, and have access to all relevant information in a timely manner. Balancing the benefits of such a standard master policy with the need for some flexibility also allows for shorter policy documents provided to clients as the details would be covered by the master policy. A master microinsurance policy provides clients with the information needed for understanding basic product features and process issues such as how to make a claim and simplifies the work of the supervisor in reviewing regulatory compliance.

The Peruvian microinsurance regulation defines product features, certain administration features, and intermediation, and allows microinsurance to be sold through aggregators such as an employer, trade unions or microfinance institution (see Box 8).

Rules for the claim payment process that work for the low-ticket sizes of microinsurance. Provisions for claims administration of insurance products can be found in the microinsurance regulation of Peru and the Philippines. In Peru, the 10 days for the claims payment are not difficult for the insurers to comply with. The issue lies at the client side, as presenting the complete documentation usually required in other insurance policies is onerous for consumers (Box 7).

Redress mechanisms for complaints should be affordable, efficient and effective and work for all, not only better-off consumers. The Philippines, through a public-private technical working group, is in the final stage of completing the development of a microinsurance redress mechanism called ADR (alternative dispute resolution). The framework uses the principles of LAPET (less cost, accessible, practical, effective and timely) mechanisms for ADR.

D – Intermediation: Sales through non-traditional agents can allow a wider range of actors and intermediaries to participate, ultimately increasing access. Relying on traditional agents, or making microinsurance agents accountable in the same manner as traditional agents and subject to the same regulatory requirements is not necessarily effective. As increasingly more “unconventional” delivery channels and agents enter the market, the lack of clear, appropriate standards applying to those selling microinsurance policies can become a problem, especially when those channels reach out to individual clients (rather than groups) who have no peers and trusted organisation they could ask for assistance.

The microinsurance regulations of **India, Peru, Mexico and South Africa** contain provisions that allow non-traditional intermediaries to assist in the sale and delivery of policies, claims administration, and other functions without the strict licensing requirements intermediaries in the traditional insurance space are subject to.

E – Other regulation: Other regulatory fields can also impact consumer protection for the microinsured. Among those are competition rules that can also help protect consumers indirectly by giving them more options and by using market forces to drive quality, price, and service improvements. Hence, some clauses in overall insurance regulation are particularly relevant to microinsurance, such as the definition and prohibition of anti-competitive practices such as collusion and price fixing. Another example is know-your customers regulation that needs to be tailored to the low-income segment; such regulations can add substantially to transaction costs and can exclude some low-income consumers who are unable to procure the appropriate documentation.

F – Supervisory practices: With consistent and effective oversight by the insurance supervisor, providers are more likely to adhere to existing prudential and market conduct rules and have in place procedures and systems to deal with the possibility of fraud or abuse more effectively, minimizing the risks and the costs for consumers. Such oversight is particularly important in microinsurance because, as noted earlier, solving problems can be proportionately more difficult and costly for poor customers than for high-income and more financially sophisticated clients. As a result, preventive rather than corrective actions are vitally important in markets serving low-income consumers, as the need to avoid problems in the first place is greater.

- **Risk-based reviews of microinsurance product components and procedures by supervisors** can help ensure that insurers implement fairly exclusions, documentation and disclosure requirements, and other controls that are appropriate and proportionate while protecting consumers from unduly burdensome requirements or exclusions.

- **Reviewing premium payment and lapsation policies and policies surrounding cash value of long-term products** ensures that financial aspects are explained in a way the low-income consumer can understand.

- **Reviewing samples of microinsurance marketing materials** is easier than requiring the supervisor's approval of all materials, which may delay implementation and cause frustration on the part of insurers. Reviewing samples can help ensure that materials are not misleading that they contain information consumers need to make informed choices, and that information is presented in a clear and accessible manner. This practice requires supervisors to develop guidelines for microinsurance materials. However, care should be taken that these guidelines are not overly rigid but allow for flexibility and innovation by focusing on desirable principles.

- **Enforcing minimum standards for complaint resolution mechanisms and tracking and**

Box 8: Microinsurance Regulation in Peru (2009)

Specifications were included on what a simplified policy document for microinsurance should entail:

- the insurer's name and address;
- the name, identity number, date of birth and address of the insured;
- details of what is covered and what is excluded;
- the procedure for claiming;
- the deadline for payment of the claim;
- the procedure for claiming and
- the complaints procedure

The regulation states the right of the policy holder to request a full policy document, to be delivered to them by the intermediary within 15 days of the request being made, allows that claims can be paid to the agent or directly to the policy holder; and stipulates that complaints must be addressed by the insurer within 15 days. The regulation also obliges to inform the client in case that there is insurance cover for a loan.

analyzing complaints statistics as an input in the supervisory process are powerful tools for supervisors to identify and address weaknesses in an insurer's procedures.

An increasing number of countries have developed a dedicated microinsurance regulation applying to prudential and/or market conduct. There is only some aggregated information on the steps that have been taken in terms of adapting supervision to the specific features of microinsurance. For example, in the Philippines, a performance monitoring framework has been set up. The South African Reserve Bank is in the process of establishing a dedicated microinsurance department. The financial supervisors in India, Peru and Mexico are monitoring their microinsurance portfolios as part of their normal supervisory practice.

5.4 Strategic options at policy level

The authors emphasize the crucial role insurance supervisors play in making their markets inclusive, for which consumer protection frameworks also need to work for the un- and underserved. In overall terms, regulators, supervisors and policymakers should work toward:

- **Striking a sound balance between adequate protection and over-regulation that creates barriers or exclusion:** In any case, regulation should be flexible enough to allow for innovation in the market while ensuring good market conduct and financial stability. In an enabling and clear regulatory framework, authorities should reduce or eliminate outdated, overlapping, or unnecessary rules and look to continually improve and modernize supervisory practices accordingly.

- **Building capacities and securing sufficient financial and human resources** for inclusion work. Such efforts can aim to improve understanding of the low-income segment, support research and data collection to support policy and supervisory decisions, ensure coordination among government bodies, train staff, exchange lessons with other jurisdictions and adapt internal systems.

- **Making the right strategic choice in terms of possible regulatory interventions and their sequencing:** either adjusting their prudential frameworks to accommodate informal players if there are significant informal operations in their jurisdiction or improving market conduct regulation to accommodate microinsurance. It is important to avoid regulations and practices that undermine the business case for providers or increase costs for consumers. Regulation should be flexible enough to allow for innovation in the market while protecting low-income consumers. Efficient supervision of this type of operation is also imperative.

- **Fostering consumer education:** Financial consumer education is an important element to be pursued in by both authorities and the private sector. However, education is not a substitute for regulation to promote fair, transparent and adequate products and practices Priority should be given to the deployment of robust supervisory interventions accompanied by effective enforcement to create fair, transparent financial products in markets that operate with integrity. Financial education programs will then have a better chance of promoting confident, self-determined financial consumers. The responsibility to educate financial consumers should not be assumed by either policy-makers or the industry alone; each one has a role to play and their interaction can and should result in more effective overall effort.

- **Looking at complementary factors** such as inter-agency coordination and cooperation with other authorities, maintaining dialogue and coordination with the private sector as well as advancing work on international standards and guidance will lead to a more effective national »RSP« framework.

6 Conclusions

As a consumer progresses through the seven steps in the insurance process, he encounters challenges and pitfalls at each step that can cause him to stumble, substantially reducing (or even totally eliminating) the value the product has to him. At each step, both industry and regulatory/supervisory players can play an important role in ensuring that the consumer is adequately protected and able to benefit from microinsurance. In light of the lessons explored in Sections 4 and 5, we revisit the consumer protection aims of each of the seven steps, highlighting measures that both industry and government/policy players can take to help ensure that each of the aims is met:

1 **Consumers have the information and financial capability needed to make an informed choice about whether to purchase insurance.** This can be best supported by broad financial literacy efforts, often led by government bodies, which give low-income consumers the tools they need to evaluate the risks they face and how best to manage those risks. While insurers and insurance industry associations can also play an important role in informing consumers about how insurance works and the role it may play, other bodies may be best equipped to present insurance within the wide range of risk management tools, enabling consumers to make informed, reasoned choices between these tools.

2 **Consumers have access to and the ability to choose understandable, affordable and valuable products.** Insurers and intermediaries, led by clear and appropriate regulatory standards, must first offer valuable, appropriate microinsurance products and also provide the information consumers need to make choices between products and providers. Both industry associations and regulators can work to develop standardized products and policy documents, making it easier for consumers to compare. The benefits of such standardization, however, must be balanced against the potential barriers to innovation by insurers. Marketing and outreach efforts must strike a fine balance between providing sufficient information to enable informed decisions and too much or too detailed information, which can be distracting or overwhelming. Because of their different relative strengths, various stakeholders can provide important checks in finding this balance. Insurers are most familiar with the most important product features and perhaps with the features most likely to be misunderstood; delivery channels are often closer to the low-income market and as a result understand the types of messages that are most likely to resonate with and be understood by low-income consumers; regulators and supervisors have the capacity to standardize the types of information that must be shared with consumers and the methods for doing so.

3 **Trustworthy and financially sound providers and additional protection in the event an insurer suffers a financial collapse.** Regulators and supervisors should take the lead in establishing prudential standards that are both sufficient to manage for the risks faced by an insurance provider (which are typically lower for microinsurance than traditional insurance) and lenient enough not to exclude providers from regulation altogether. In accordance with IAIS principles, insurance providers should generally be licensed and subject to prudential standards. Given the prevalence of informal (unlicensed) microinsurance providers throughout the world, it is crucial for supervisors to develop transitional arrangements to incorporate those providers into the regulatory system over time.

4 **Sales processes that are appropriate and accessible for microinsurance consumers, allowing them to make informed purchase decisions.** Consumers' ability to understand the products they purchase (on either a mandatory or voluntary basis) relies on an adequate explanation of the product, either verbally or through a policy document.

Simple underlying products are far easier to explain in a straightforward manner, minimizing the chance of confusion. Regardless of the complexity of the product, however, the delivery channel plays a vital role at this stage. However, those selling insurance and enrolling clients often face conflicting incentives and limited capacity. Here again, various other parties can provide important support. Regulators can set limits on sales tactics, establish licensing and training requirements, and proscribe certain standard disclosures. Insurers can provide additional support through training and providing accessible policy documents and other materials. Insurers should also be held accountable to a great extent for the actions of those selling insurance on their behalf, creating incentive for insurers to provide checks on intermediaries' actions. The role of insurers in sales and enrollment processes is particularly important where non-traditional (and often unlicensed) intermediary channels are used.

5 Appropriate and transparent payment and renewal procedures and adequate after-sales customer care. Simple, straightforward processes are easiest to understand and explain and least likely to mistakes or misunderstanding by the consumer. As such, insurers and delivery channels (to the extent they are involved in payment and renewal) should strive for simplicity. Regulatory standards help to ensure that important details about consumers' ongoing rights and responsibilities are made clear, helping to avoid the risk of either an unintended lapse or an unintended renewal of a policy.

6 Claims processing that is straightforward and prompt. Claims procedures and documentation requirements should be as simple and cheap as possible from the consumer's perspective to adequately meet insurers' needs to avoid fraud. Prompt payment of claims is also a crucial component of consumer protection in microinsurance and relies on both quick processing and payment after documentation is submitted and accessible documentation requirements that allow consumers to submit claims in a timely manner. Regulation can easily set standards for the former, but the more nuanced issues involved in documentation requirements may be best evaluated by insurers, with some oversight from the supervisor.

7 **Accessible and effective complaints and redress options in the case of a conflict.** Insurers and/or delivery channels should maintain an accessible complaint resolution process and make consumers aware of its existence. Consumers should also have access to some mechanism for external appeals in the event a dispute is not resolved internally, which may be led by government and/or industry bodies.

Further Readings

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