Technical Note 1

access to insurance initiative

Evolving microinsurance business models and their regulatory implications[1]

Context: Insurance supervisors face an increasing variety of business models in microinsurance. Supervisors need to understand which business models prevail in specific product markets leading to new consumer protection risks, as well as regulatory responses to these risks in various jurisdictions. The **nature of distribution characterises** these business models because insurance is typically sold and not bought. Insurers need to innovate in the area of distribution, because microinsurance premiums and margins are low, therefore insurers need to scale up quickly to become viable. In addition insurers face particular challenges in reaching out to the low income market due to limited infrastructure, poor connectivity, and low education levels coupled with clients' limited experience with insurance. The synthesis paper identified eight business models:

Model	Description
Individual sales	Insurance sold on a one-on-one basis through dedicated registered or licensed insurance agents or brokers.
Proxy sales force	Insurance is sold to existing clients of a non-insurance entity (client aggregator). Salesperson works for the aggregator. Insurance is marketed with the primary good they sell.
Compulsory insurance	Certain categories of citizens are compelled by regulation to purchase/contribute to prescribed risk covers.
Group decision	Members of a group become policyholders by virtue of belonging to that group. The group policy is negotiated collectively.
Local self-help	A group of persons (such as a mutual or another community-based organisation) pools its own risks.
Auto-enrolment	A third party purchases insurance on behalf of policyholders. The state may subsidise insurance or a mobile network operator may purchase insurance for its clients as a loyalty scheme.
Passive sales	An individual purchases insurance without a sales person, for example through a retailer, responding to mass marketing or a mail shot campaign, or online.
Service-based sales	The client secures a service to be rendered in the future through an insurance policy. The entity which sells the insurance is the same one that provides the service.

Challenge: How can supervisors mitigate consumer risks in microinsurance business models while at the same time allowing for innovative distribution channels? Different business models give rise to different combinations of consumer protection risks. Consumer protection needs are heightened in distribution channels that are enclosing large groups, and involve non-insurance parties, which are not regulated under the insurance law. The **nature and intention of the "client aggregator"**[2] comes with a major benefit, as the aggregator often brands the product and therefore needs to assure quality, but pitfalls as well, i.e. when the aggregator defines the cover. Such insurance tends to be driven by non-insurance business motives, strengthening the distributor's core business or creating additional revenue. Products may focus on the distributor-related risks, rather than the clients' priority risks, such as in the case of a utility provider who insures cover for two months of bill payment. Aggregator's staff incentives can also be misaligned, or staff accountability or oversight can be inadequate, especially if staff has insufficient knowledge and skills. When insurance is embedded or part of a group policy, policy awareness can be low. Clients may face unreasonable barriers after the sale to maintain or change their cover, make enquiries or submit claims. Moreover, where clients have little understanding of insurance, and few resources to access consumer recourse mechanisms, traditional recourse mechanisms are often out of reach. The synthesis paper identifies six **consumer protection risks**:

[1] This note highlights key findings from the full synthesis paper available at: [http://www.a2ii.org/document-details.html?dam_single=2941].

[2] A "client aggregator" can be e.g.: retail shops, post office outlets, credit providers, community groups, pharmacies, trader associations, mobile network operators, agricultural processors, labour unions, cooperatives, and utility providers.

Prudential Risk	Aggregator Risk	Sales Risk	Policy Awareness Risk	Payments Risk	Post Sales Risk
Risk that insurer is not able to keep its promises and deliver the benefits to the beneficiaries.	The risk of reduced client value and inappropriate products being sold to clients when an insurer accesses the aggregated client base of a non-insurance third party to sell its products through that channel.	Risk that the salesperson will misrepresent the product to the client or sell a product that the client does not need.	Risk that the insured is not aware that he or she has an insurance policy and is therefore unable to lodge a claim should the risk event occur.	Risk that the premium will not reach the insurer, that the premium will not be paid on the due date or that the cost of collecting the premium is disproportionate.	Risk that clients face unreasonable post-sale barriers to maintain their cover, change products, make enquiries, submit claims, receive benefits or make complaints.

Messages for supervisors: Across jurisdictions insurance supervisors have been developing regulatory and supervisory responses which address the various consumer protection risks. Supervisors have tailored regulations to the particular challenges in microinsurance, i.e. the nature of the client, and their needs, and the alternate channels that are close, trusted and hence, should work for these clients. Supervisors for example require:

- Product restrictions for microinsurance on limits for maximum cover or premium, term or risks that may be covered
- Product approval for microinsurance products
- Product simplification, for example plain and vernacular language and limited exclusions
- Disclosure of the service agreement between the insurer and the distributor
- Explicit disclosure requirements, that is, minimum terms and conditions to be disclosed to the client verbally and/or in writing, often in the client's vernacular
- Minimum qualifications and obligations of dedicated agents or other sales persons selling microinsurance
- Caps on aggregate distribution costs
- Mandatory choice between various insurers in the case of compulsory cover
- Cooling-off periods within which the client can withdraw from the contract
- Mandatory post-sales communication
- Performance standards for microinsurance, including claims and expense ratios

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

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

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