Opportunities and challenges presented by alternative distribution channels

8th Consultative Forum on inclusive insurance regulation for insurance supervisory authorities & insurance practitioners; Thursday, 1st December 2016; San José, Costa Rica.

New distribution avenues challenge supervisory practices. Distribution is key to providing suitable insurance coverage to low-income and excluded populations. As insurers are faced with low profit margins, they need to find low-cost channels that can reach large numbers of clients, while making sure that the client is properly informed about the product. Alternative distribution channels operating as client aggregators include all kinds of non-traditional intermediation modes such as e-money providers or non-financial intermediaries such as retailers, utility companies or Mobile Network Operators (MNOs). Many of them act as a group policyholder and some of these business models involve a third party, e.g. a technical service provider (TSP), who assumes various functions from product design to claims administration. Some TSPs are even licensed as intermediary, often using call centres and own sales staff or agents for distribution. This results in a more complex value chain with a variety of insurance and non-insurance stakeholders involved that assume different roles. The longer value chain often comes with a power imbalance against the insurer being the client aggregator and the party that dominates the client relationship, hence the partnership. Commissions in alternative distribution vary considerably, ranging from 10% to 60% with a median of around 30%. All these challenge traditional supervisory approaches in multiple ways.

Technology drives the distribution of inclusive insurance services. Digital financial services (DFS) are used to undertake different types of financial transactions, including basic cash in/out, payments, transfers, savings, investments, credit, pensions and insurance. Mobile banking, internet banking and mobile wallets are the most widely employed technology-driven distribution channels. MNOs are strong drivers, bringing their mobile phone client base to the partnership, or driving e-payments; e-money providers are often subsidiaries of MNOs. In Honduras, an insurance intermediary uses MNOs as a distribution channel and client airtime to charge premiums. Deductions can be made on a monthly or daily basis, which allows clients to pay premiums according to their cash flows. This would not be viable for an insurer due to the cost of each payment transaction. In addition, electronic signatures are valid in Honduras, which greatly benefitted people especially those living in remote areas. Digitally supported insurance helps in lowering costs, overcoming physical infrastructure barriers, extending outreach, and offering more convenient and faster transactions, and hence can be a key contributing factor to more and better inclusive insurance.

Innovative practices are emerging. Peer-to-peer insurance models are emerging and driving customer adoption and satisfaction. In order to reduce costs of insurance covers and the inherent conflict between insurance providers and policyholders, especially at the time of a claim, the peer-to-peer concept was created. A key aspect of the model is to reward small groups of users with a cash-back bonus at the end of the year should they remain claimless. **Blockchain technology (BT)** allows efficient data storage and insurance transactions. A lot of valuable information is stored in the central databases of insurance companies and their intermediaries. The organisation who owns the database controls the data and when the database fails, there is no access to the data anymore. As a result, central databases are heavily protected, both physically and digitally, which renders data storage and usage expensive in the long run. BT may overtake both the role of the insurer as well as the intermediate and support data storage and sharing. This is especially true for simple insurance products. BT may be able to help insurers reduce

"Insurers and regulators should recognise the importance of sustainable products for the low-income people and farmers."
Tomás Soley,
Superintendencia General de Seguros de Costa Rica (Sugese), Costa Rica

"The input for the development of appropriate regulations comes from conferences like this and from participants like you. We learn lessons and apply them directly in our supervisory material."
Conor Donaldson,
International Association of Insurance Supervisors (IAIS), Switzerland

"Blockchain is specifically tailored towards simple products, for instance to create a proof of cover that gives you access to treatment in a hospital."
Michiel Berende,
R*ISKebiz,*
The Netherlands

"As supervisors and regulators, we develop strong links with insurance companies to stimulate them to sell both mass insurance and inclusive insurance via the right channels."
Mirla Barreto,
Superintendencia de Banca, Seguros y AFP del Perú (SBS), Peru

overhead costs by making simple products automated in terms of underwriting and claims payment.

Retailers, direct sales and call centres are predominant distribution channels in Latin America and the Caribbean Region (LAC). In an effort to reduce administration costs and increase efficiency, distribution in LAC often relies on call centres. Call centres support customer education and provide customer services for a number of insurance products including simple health, life and property products. In Honduras, one insurance intermediary has a quality control department in place that ensures that (call centre) agents properly explain to the clients how the products work and how to make a claim. In Mexico, call centres also often help to handle claims. Another alternative distribution channel offering inclusive insurance in Mexico are grocery stores. One of the success factors of this business model was the fact that most customers already had a credit account with the store. This sped up the selling process as customer data was already in the system and consumer enrolment was quick. The life product sold through the store showed acceptance rates of 50%. In Costa Rica, call centres need at least 13 minutes to sell an insurance policy because of the amount of information they are required to convey based on their insurance regulation. However, the average caller loses interest in the call after 7 minutes. This is because the agent is sometimes explaining insurance and not only the product per se.

Challenges for the industry. The fact that insurance is only an add-on for alternative channels can come with reputational risk when servicing is weak or a product is withdrawn. Some insurers feel that their reputational risk is also increasing due to the increasing use of social media and websites. Even if insurers explain the product very thoroughly and apply a diligent claims assessment, unsatisfied clients vent their anger online and increasingly challenge the insurers' decisions. One way to address this is to allow insurers to point to publicly available policy documents, questions and answers (Q&A) and similar sources of clarification e.g. on a website or guide customers to where they can find them. What often occurs is that the insured or beneficiaries are not aware of having coverage and hence, claims ratios remain very low; agent incentives (as for example in Mexico) for identifying such cases helped to improve this situation. Agent training requirements are reported to be one of the most important aspects to improve trust and viability of the business model. Online training for larger numbers of sales staff or agents is an important low-cost option but face-to-face training is still required.

Challenges for consumers. Consumers are faced with a number of challenges while taking up insurance products via alternative distribution channels due to low insurance awareness and understanding coupled with a lack of digital skills. There is a real concern that less digitally acquainted individuals, as well as rural, older and low-income segments of the population may be missing out on important insurance information. Consumers may not be able to manage their insurance when it is supported electronically. They may purchase insurance but do not understand what it does or how to use it.

Challenges for regulators. In order to protect consumers' interests while at the same time creating a level playing field for insurers, intermediaries and alternative distribution channels like MNOs or retailers, regulations need to be flexible enough to accommodate such innovative business models which often rely on the support of the mobile phone and increasingly the internet. Regulatory capacities may not be sufficient to update regulations and supervisory tools keeping up with the pace of technological advancements including ensuring cyber security.

"The concepts and innovations of FinTech are allies in providing better access to insurance and coverage which regulators have to understand in order to offer a suitable regulation."
Recaredo Arias, *Association of Mexican Insurance Companies (AMIS)/Global Federation of Insurance Associations (GFIA), Mexico*

"In Mexico, the agents were encouraged (and rewarded) when they explored whether or not the person had an insurance with his/her loan."
Martha Gómez, *Seguros Monterrey, Mexico*

"Re-thinking distribution is key to successful inclusive insurance. Low distribution costs make insurance affordable for low-income people."
Peter Wrede, *World Bank Group, USA*

"Education and market transparency are important. Do not try to transport an elephant in a Volkswagen. Either have another car or another animal."
Tomás Soley, *Superintendencia General de Seguros de Costa Rica (Sugese) , Costa Rica*

Key takeaways and recommendations for action to the industry

- Keep products simple and insurance transactions transparent for the end client.
- Ensure insurance education during marketing, keeping in mind that the client has insurance for the first time and may not be acquainted with digitalisation issues.
- Improve the value of product offerings through digital solutions while ensuring data protection and cyber security.
- Be aware of the necessity to continuously enhance and monitor the know-how of agents, sales staff and call centre staff of the alternative distribution channels.
- For these simple products, rapid claims payment within less than five days is feasible and helps to improve trust in insurance.
- Multiple communication approaches using call centres, websites and SMS can optimise interaction between the insurer or intermediary and the insured.

Key takeaways and recommendations for action to regulators

- Train all relevant supervisory staff in technological issues, not only those in the information technology department.
- Adjust regulatory requirements and supervisory tools to keep up with the pace of technological advancements in areas related to e-documentation, effective disclosure and agent training requirements.
- Oversee the various stakeholders in the value chain; requiring insurers to have adequate controls in place for parties to which services are outsourced, such as alternative distribution channels and call centres.
- Develop ways to inform the public about insurance by way of contributing to transparency; e.g. publishing complaints statistics, and supervising comparison websites that publish prices.
- Instead of limiting commissions, alternatives should be considered such as requiring adequate transparency on the features and cost of products, and enabling a broad range of channels to foster competition between aggregators.
- Insurance education programmes should also focus on digital skills to help prepare policyholders and beneficiaries to understand and use new technologies. They should be designed involving the beneficiaries to make them effective.

"Trust comes on foot but leaves on horseback."
Peter Wrede, *World Bank Group, USA*

"Give thought to whether the insurance needs to be a separate voluntary product or a mandatory part of another core product.
Carlos Boelsterli, *MiCRO, USA*

"In Peru, NGOs are the only entities that successfully reached out to the low-income people with products they need and understand."
Mirla Barreto, *Superintendencia de Banca, Seguros y AFP del Perú (SBS)*