access to insurance initiative

Making insurance markets work for the poor: microinsurance policy, regulation and supervision

Colombian case study

BILL & MELINDA GATES foundation

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This document presents the findings from the Colombian component of a five-country case study on the role of regulation in the development of microinsurance markets. The objectives of this project were to map the experience in a sample of five developing countries (Colombia, India, the Philippines, South Africa and Uganda) where microinsurance products have evolved and to consider the influence that policy, regulation and supervision on the development of these markets. From this evidence base, cross-country lessons were extracted that seek to offer guidance to policymakers, regulators and supervisors who are looking to support the development of microinsurance in their jurisdiction. It must be emphasized that these findings do not provide an easy recipe for developing microinsurance but only identifies some of the key issues that need to be considered. In fact, the findings emphasize the need for a comprehensive approach informed by and tailored to domestic conditions and adjusted continuously as the environment evolves.

The project was majority funded by the Canadian International Development Research Centre (www.idrc.ca) and the Bill and Melinda Gates Foundation (www.gatesfoundation.org) along with funding and technical support from the South Africa-based FinMark Trust (www.finmarktrust.org.za)[1] and BMZ[2] (www.bmz.de). FinMark Trust was contracted to design and manage the project. Together with representatives of the IAIS, the Microinsurance Centre and the International Cooperative and Mutual Insurance Federation (ICMIF) the funders are represented on an advisory committee overseeing the study. The project was undertaken under the guidance of the International Association of Insurance Supervisors (IAIS) and Consultative Group to Assist the Poor (CGAP) Joint Working Group on Microinsurance.

The Colombian case study was conducted by PrimAmerica (www.primamerica.cl) and Fedesarrollo (www.fedesarrollo.org).

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Executive Summary

Context

Over the past two decades Colombia has experienced financial liberalisation and growth, but also a major financial sector crisis. Against this backdrop, the country has seen significant microinsurance development, traditionally through its large cooperative insurers and more recently also on the back of microfinance development. This is made all the more remarkable as there is no microinsurance regulation and only indicative financial inclusion policies. Colombia therefore illustrates that microinsurance can develop where external circumstances are favourable and where the policymaker and regulator have a fairly open stance, even without a dedicated microinsurance regime. Yet uniform prudential requirements mean that it remains difficult to provide microinsurance “from the bottom up”.

In the early 1990s, the Colombian government embarked on a comprehensive economic liberalisation process that included trade and financial liberalisation measures, the independence of the central bank and the end to its monopoly on foreign exchange transactions, as well as various fiscal and public sector reforms. This laid the foundation for an average growth rate of almost 6% between 1991 and 1995. With the reforms however also came an imbalance on the current account and a fiscal deficit – factors that made Colombia vulnerable to the spillover effects of the Asian financial crisis at the end of the 1990s. The subsequent financial sector crisis saw the banking sector lose 40% of its equity and GDP contract by 4.2% in 1999. In the insurance sector, the impact was less severe and no insurers failed during the crisis. Post-crisis, government strengthened financial sector regulation and in 2006 a new financial regulatory agency, the Financial Superintendence, was formed by merging the agencies in charge of supervising financial institutions and securities.

Insurance premiums per capita are relatively low compared to other Latin American countries. Surprisingly low is the penetration of life insurance, which accounts for only 11% of total premiums. It is suggested that this low figure is in part due to the fact that traditionally high-income individuals tended to obtain insurance abroad (even though it is in contravention of the Colombian insurance law[3]). The share of life insurance is however on the rise (premium growth amounted to almost 24% in 2006), driven largely by improved macroeconomic performance and hence lower inflation rates since the turn of the century. In addition credit life insurance has shown significant growth recently. This is the result of the quest for micro-credit expansion by formal financial service providers, a movement catalysed by financial liberalisation (that increased competition and led to a reduction of margins in traditional segments of the market, thereby prompting commercial banks to enter lower-income markets in search of new clients), and further spurred by government’s

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[3] The insurance law, the FLFS, requires foreign companies to set up a local subsidiary in order to sell policies locally. This phenomenon, the result of a high inflationary environment, was most prevalent in the 1970s and 1980s in Colombia, but is now on the decline.

financial inclusion policy ("Opportunity Banking") implemented in 2006. Therefore, despite the fact that usage of formal financial services is estimated to be as low as 34% of the population[4], the Colombian financial sector has recently experienced a distinct move down-market.

Salient features of the microinsurance market

Usage. An estimated 19% of Colombian adults are microinsurance clients. There are about 2.74m[5] formal microinsurance policies (9% of the adult population). Informal microinsurance (most notably funeral insurance provided by so-called funeral entities) also plays an important role. Industry sources estimate the informal market to reach up to 3m clients (10% of adults), making it slightly bigger than the formal market (at 52% of the total microinsurance market).

Players. There are 43 registered insurers in Colombia of that 41 are corporates and two are cooperatives. Though 17 insurers provide some form of microinsurance products, the two insurance cooperatives, La Equidad and Solidaria, are the microinsurance pioneers and remain the largest players in the microinsurance market. With their 1.7m insurance policyholders, they are estimated to account for 62% of the total formal microinsurance market. This is however still significantly below the total cooperative membership of 3.7m, implying scope for further cooperative-based microinsurance expansion.

Products. Voluntary microinsurance plays an important role in Colombia compared to international experience. Compulsory credit life insurance is currently estimated to account for only 27% of all microinsurance clients, though it is growing strongly on the back of credit expansion. The most popular life microinsurance products are funeral insurance, followed by credit life insurance. Innovative new products are also increasingly marketed on the non-life side, including motorbike insurance, insurance tailored to cover the stock of small businesses, repatriation insurance for migrant workers, products providing benefit pay-outs in the form of grocery vouchers or education fee coverage, and cell phone insurance. Fasecolda (the insurance industry association) estimates property insurance to comprise 60% of the microinsurance market. This category is in turn largely made up by cell phone insurance. 30m Colombians (about 64% of the population), 72% of whom are classified as lower income, now own a cell phone.

Distribution. Traditional broker and agent distribution channels do not feature prominently in the microinsurance market. Instead, microinsurance is distributed largely through cooperatives, as well as through micro-credit NGOs requiring compulsory credit life

[4] National Banking Association Survey, 2007, as quoted in country report. Note that this figure may be overestimated, as it is not clear that the actual number of account holders, rather than accounts, was measured. There may be some duplication of accounts per person.
[5] This may be a slight overestimation of policyholders, as some people may have more than one policy.

insurance. Direct sales[6], bancassurance and distribution through utilities[7] are also emerging as important intermediation channels.

Additional channels such as hospitals, educational establishments, large retail outlets/networks and funeral homes could also become significant, though such distribution is not found at the moment, except for a recently launched initiative where life insurance is sold through cashiers at some supermarkets. The potential of cell phones to support distribution in the low-income market is of yet untapped.

The insurance policy, regulation and supervision landscape

Colombia has no dedicated insurance law. Insurance is incorporated with other financial activities under the Fundamental Law of the Financial System (FLFS) and its subordinate decrees and regulations. The Financial Superintendence (FS) acts as insurance regulator and supervisor.

Prudential and institutional regulation. Both public corporations and cooperatives may register as insurers. The minimum upfront capital requirement consists of a standard minimum capital component, as well as additional technical capital requirements per class of product provided. In 2006, the standard component was \$2.7m for life and non-life insurers, \$1.5m for credit and export insurers, and \$ 11m for reinsurers. The technical equity required ranges from \$0.3m to \$1.2m, according to the type of product. Therefore the total minimum upfront capital requirement will depend on the combination of products provided by the insurer. Apart from the FLFS, Law 79 of 1988 on Cooperatives is also of relevance. It establishes a framework to develop cooperative activities and allows cooperative insurers to provide insurance to non-members. There is no special dispensation for cooperative insurers and they have to adhere to the full set of regulatory requirements for insurers.

Product regulation. Upon registration insurers are authorised to provide various classes of policies (group life, health, vehicle, asset, etc). New products have to be submitted to the FS, but no product authorisation is required. Strict product demarcation applies only to individual life policies. Under Article 38 of the FLFS, insurers providing individual life policies must do so exclusively. Any other life insurers may sell group life, collective life[8], health, personal accident, funeral or education policies, as well as annuities and non-life policies. Non-life insurers may sell collective life, group life and health insurance in addition to asset-based policies.

Market conduct regulation. In Colombia insurance may be distributed directly by the insurance company, through agents, insurance agencies or by means of insurance brokers.

[6] "Directs sales" refer to insurance products sold directly by the insurer without tied agents or brokers, for example through telemarketing, direct mail, or call centres. Sometimes this involves insurers selling products through their employees without such employees being considered agents or brokers. This is allowed under Art. 5 FLFS and Art 2 Decree 2605, 1993.

[7] With the insurance premium added as a separate item to a person's monthly utility statement

[8] The only difference between group life and collective life policies is that in the former there is some relationship between the policyholders, for example they belong to the same union. Collective life would for example refer to the policies sold via the electricity utility.

Under the Cooperative Law, insurance cooperatives may sell their own or another insurer's policies without the use of agents, brokers or agencies. The main difference between brokers and agents is that while agents are natural persons, brokers must be a limited company or public corporation. They must register with the financial superintendence and are subject to capital requirements. Agents do not have to register and the onus is placed on the insurers dealing with them to ensure that they are compliant and competent. Insurers must certify that they have trained their agents to ensure that they will be competent and must make their training programmes available to the FS. In practice, insurers implement this requirement jointly through courses presented by the industry association, Fasecolda.

The direct distribution and agencies channels are interpreted quite broadly to accommodate new channels. New channels (for example bancassurance or distribution through public utilities) have also been regulated through subordinate regulation on an ad hoc basis. There is no price control on premiums or commissions. Market conduct provisions mostly relate to consumer protection measures such as the right to choose the provider in the case of credit insurance and the establishment of proper complaints procedures.

Financial inclusion policy. Financial inclusion is an important policy objective, specifically the president, and government invests much energy in supporting the development of financial services for the poor. A key feature is the Opportunity Banking Policy that was launched in 2006 and seeks to provide access to financial services, including payments, transfers, savings, loans, insurance, pensions and remittances. It does not place any regulated inclusion objectives on private financial institutions, but establishes the overall policy framework that guides public and private players to extend access to financial services. Amongst others, the government has amended banking regulations to allow the establishment of non-bank agents (named "non-bank correspondents") to extend the formal banking network into previously unserved areas. As of June 2007, there were 3,508 non-bank correspondents and between 2006 and 2007 the new channel has enabled almost 1m Colombians to access formal credit for the first time. Non-bank correspondents are not currently allowed to sell insurance (though they may collect premiums).

Drivers of microinsurance development

Market related drivers

Two main market forces have driven the development and state of the microinsurance market in Colombia:

- The increasing competition resulting from the financial liberalization carried out in the early nineties forced banks and insurance companies to look for a new niche market in the low income market segments. This stimulated microinsurance directly, but also indirectly, through the growth effect on microfinance (which in turn stimulates credit life insurance)

- The existence of a significant cooperative MFI (NGOs as well as banks focused on micro credit) sector has facilitated the expansion of services in the low-income market.

Impact of policy, regulation and supervision on the market

As the FLFS makes no reference to microinsurance and there is no official microinsurance definition, the Colombian experience illustrates that microinsurance can grow even in the absence of any regulatory concessions to facilitate its development. However, this is only possible because general insurance regulation does not impose an unduly heavy burden on the intermediation of microinsurance; neither is it restrictive on underwriting:

- *Insurance provided by funeral entities unregulated*. Funeral entities serve a large part of the market and have also supported formal market development by increasing awareness and familiarity with the concept of insurance. A 2006 opinion by the FS (based on a 2003 constitutional court judgment) holds that the policies provided by funeral service providers fall outside the definition of insurance in the FLFS. These providers therefore operate on an unregulated and unsupervised basis. Though this "regulatory forbearance" has by and large served the development of the market, it could create the risk of consumer abuse if not carefully monitored by the supervisor.

- *Demarcation rules favourable to market development.* Market development in Colombia is supported by the fact that an insurer is allowed to provide health, non-life and group life policies under a single license.

- *Flexible market conduct regime.* The Colombian regulatory framework facilitates microinsurance intermediation in a number of ways: it accommodates new channels within the "direct sales" or "agencies" categories or through specific subordinate legislation as they arise. Furthermore, no price controls (in the form of commission caps) apply to the intermediation process. Cooperatives may sell insurance to non-members and may act directly as distribution channel. Lastly, the FS delegates supervision of agents to insurers. These factors combine to make Colombia one of the sample countries with the most flexible market conduct regime. This gives providers the confidence to pursue distribution innovation, as witnessed in the various new channels emerging.

- *Active government encouragement of low-income market activity.* To date one of the main impacts of the Opportunity Banking policy has been the introduction of "non-bank correspondents" as an intermediary category to support the distribution of financial services in poor and remote areas. The expansion of micro-credit in turn paves the way for credit life microinsurance expansion.

Conclusion: key insights

A relatively open regulatory stance as well as generally low regulatory burden, especially on the intermediation side, has meant that market rather than regulatory forces have been the definitive driver of microinsurance development. Nevertheless, a number of policy and regulatory aspects impact on the microinsurance market. Perhaps most significantly, the Opportunity Banking Policy represents a significant push by government for the facilitation of financial inclusion. Though current evidence suggests that the absence of microinsurance-specific regulation has generally not hampered the development of microinsurance, overall microinsurance penetration remains low and microinsurance is still largely driven by two large cooperative players. The creation of a microinsurance definition may serve to align policies and efforts for the development of the market and close the regulatory gaps that do exist, such as the fact that no intermediate step or tier with reduced regulatory cost is available to smaller or community-based entities who want to enter the microinsurance market.

1. Introduction

This document presents the findings from the Colombian component of a five-country case study on the role of regulation in the development of microinsurance markets. The objectives of this project are to map the experience in a sample of five developing countries (Colombia, India, the Philippines, South Africa and Uganda) where microinsurance products have evolved and to consider the influence of policy, regulation and supervision on the development of these markets. From this evidence base, cross-country lessons are extracted that seek to offer guidance to policymakers, regulators and supervisors who are looking to support the development of microinsurance in their jurisdiction. It must be emphasized that these findings do not provide an easy recipe for developing microinsurance but only identify some of the key issues that need to be considered. In fact, the findings emphasize the need for a comprehensive approach informed by and tailored to domestic conditions and adjusted continuously as the environment evolves.

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Micro-insurance can make an important contribution to social welfare in the poorer and lower-middle class sectors. Low income families do not have mechanisms to face and handle risks that suddenly push them in poverty. International experience has shown that insurance can play an important role in risk mitigation for the lower income as well as the medium income sectors.

Micro-insurance is defined as insurance that is accessible to the low-income population, provided by a variety of different providers and managed in accordance with generally accepted insurance practices. That is, the risk should be funded by premiums and managed based on generally accepted risk-management principles. Though Micro-insurance is part of the broader insurance market, it is focused on the low income market segment.

There are many factors that make development of micro-insurance products difficult. Regulation is one of these factors because an inappropriate regulation, as well as its absence could promote or restrain micro-insurance development. Inadequate regulation could come down in high costs of entry, in high solvency requirements, in impediments to the

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[9] Funded by the UK Department for International Development – DFID.

[10] Bundesministerium für Wirtschaftliche Zusammenarbeit und Entwicklung - Federal Ministry of Economic Cooperation and Development

employment of new distribution channels and the use of new premium collecting systems, among others.

According to the Federation of Colombian Insurers (Fasecolda), in Colombia, 8.4% of the Base of the Population Pyramid (BPP), defined as those who survive with less that US$2 per day, would be covered by some microinsurance product.[11] This figure is higher than Latin America (6.8%) and Asia (2.5%). While there is reasonable doubt among some analysts as regards the Colombian figure, at the moment 41% of the insurance companies are offering Micro-insurance products. That group of companies includes domestic as well as foreign insurance companies.

The study will be focused principally on the analysis of the existing insurance regulation considering that an excess or a lack of rules can be one of the factors that inhibit the development of microinsurance. Experience has demonstrated that it is possible to get the insurance's benefit for the vulnerable sectors of the population finding efficient and low cost distribution channels and developing simple products that are easy to sell and understand and appropriate to the needs of the poor.

The end-purpose of the analysis will be to establish whether or not Colombian insurance regulations addressed to the formal insurance market are discouraging the Micro-insurance offer. At the same time, the analysis will permit an identification of those situations that could be improved in future regulations. Based on the market and regulatory analysis, preliminary guiding principles will be formulated for the Regulation and Supervision of institutions so as to facilitate the provision of micro-insurance in developing countries. The analysis excludes all social welfare mechanisms, particularly medical aid or public health insurance.

The document has six parts. **Section 2** considers the analytical framework, methodology and research approach of the document. **Section 3** provides a brief description of the Colombian economy and the insurance market. **Section 4** presents an overview of the insurance regulatory framework. **Section 5** provides a market analysis. **Section 6** presents the findings and conclusions.

2. Analytical framework

This study applies a number of lenses to the evolution of microinsurance markets in the five countries. These lenses, collectively referred to as the analytical framework, in turn inform the synthesis of drivers and findings in the cross-country report. The full analytical framework is contained in Appendix 1. It covers:

- The financial inclusion framework

[11] See Fasecolda (2007) with data of "The Landscape of Microinsurance in the World's 100 Poorest Countries", Microinsurance Centre, 2007, and The Next Four Billion, World Bank, 2007.

- The goal of microinsurance, namely increased welfare for the poor through risk mitigation to reduce vulnerability.

- The definition of microinsurance, namely insurance managed according to insurance principles, in exchange for a premium, that is accessed by or accessible to the low-income market.

- The parts of the insurance value chain covered, including underwriting, administration and intermediation/distribution.

- The distinction between formal and informal insurance and intermediation.

- The categories of risk identified, namely prudential risk, market conduct risk and supervisory risk.

- A typology of public policy instruments, namely policy, regulation and supervision.

- An overview of the insurance regulatory scheme (most notably financial inclusion policy or regulation, prudential regulation, market conduct regulation and institutional regulation)

Please refer to Appendix 1 for a detailed analysis of each of these areas.

2.1. Methodological approach

The **structure** of the analysis is as follows:

- *Understanding the microinsurance market*. The microinsurance market is described in terms of: (i) the various players (corporate and mutual/cooperative, formal and informal) active in the low-income market; (ii) the products available and any low-income market product innovations; (iii) usage among the low-income population of formal and informal insurance products; as well as (iii) distribution channels employed in the low-income market and any distribution innovations. These findings are used to conclude on the key characteristics of the microinsurance market. Focus group research was used to identify the need for and understanding of insurance among the target market. This included an investigation into the risk experience, provider, product and channel preferences of the focus group participants, as well their trust in the insurance market in general.

- *Understanding the insurance regulatory framework*. Furthermore, the study gives an overview of the insurance regulatory framework, in general and as pertaining to microinsurance.

- *Drivers of microinsurance*. In light of the above, it seeks to draw out respectively the non-regulatory (market, macroeconomic and political economy context-related) and regulatory drivers of the state of microinsurance. These drivers are synthesised in the cross-country document.

- *Conclusion*. The drivers are used as the basis for highlighting conclusions on the development of the market, the impact thereon of regulation and other factors and the way forward for microinsurance policy, regulation and supervision.

The **methodology** consisted of desktop research as well as consultations with industry role players, regulators, supervisors and other stakeholders. It involved:

- Traditional demand and supply mapping
- Qualitative focus group research
- Regulatory and policy analysis
- Controlling for context and the distinctive evolution of the broader insurance market

2.2. Project scope

The scope of the study covers all life and non-life insurance products targeted at the low-income market, including savings products provided by insurers (endowments) where it includes an element of guarantee. Pure savings products and retirement savings products are excluded from the scope of the study, as is government social welfare and social security provision.

While capital health insurance products are considered, indemnity health insurance was excluded from the scope of the study. Indemnity health insurance is an extremely important product for the low-income market but requires a dedicated study as it is often regulated and supervised differently to other insurance business and is a complex field, intricately linked to health service provision.

The study covers all categories of providers and intermediaries, including informal markets.

3. The Colombian economy and the insurance industry

3.1. The Colombian Economy

Colombia undertook an economic liberalization process in the 1990's that laid the foundations for the economy to exceed its historic growth levels. The average growth rate between 1991 and 1995 was 5.7% per year.

However, at the end of nineties Colombia bore its worst economic crisis in 30 years. This crisis was a result of internal and external factors. In the domestic context, Colombia experienced a political crisis and a deep financial crisis, resulting from the rise in interest rate that took place simultaneously with the fall in economic activity. At the same time, the security situation was made worse with a consequent negative impact on investment. This fall in investment was reinforced by the international financial crisis.

In 1999 the GDP contracted 4.2% (Figure 1). As a result of the poor economic performance and weaknesses in regulation and supervision, the financial sector entered a period of crisis.

The non-performing loans/total loans ratio in the banking sector went from 6% before the crisis to 16% at the end of 1999. The sector's losses represented almost 40% of the system's equity between 1998 and 2000 (Salazar, 2005). Housing and government-owned banks were particularly affected by the financial crisis, but it also had a negative effect on the financial cooperative sector. The economic recession was accompanied by a credit stagnation phase and the gains in financial deepening achieved between 1990 and 1997 were practically lost.

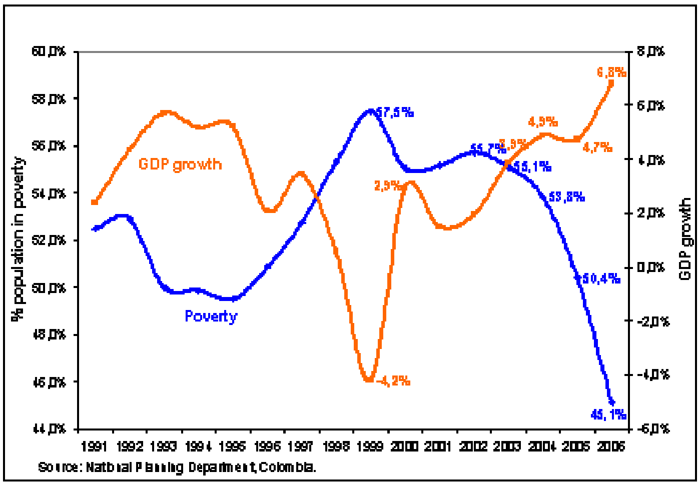

Figure 1 . Colombia: GDP and population in poverty

As a result of the crisis, the government undertook a bailout process and strengthened regulation of not only financial entities but also financial cooperatives. The housing entities, that provided mortgages, were merged with banks and some cooperative banks disappeared, but the business model implemented in the financial sector in the early nineties was maintained. At the beginning of the 90's law 45/1990 adopted a "multi-banking" system (introducing the concept of matrix-subsidiaries) that permitted equity participations between some financial institutions. This reform promoted the creation of financial conglomerates (see Section 4.1).

The economic crisis also had an impact on insurance companies; however premiums have showed a sustained increase since 1997. After the crisis the insurance companies have had a positive performance, and non-life insurances grow at a faster rate than life insurances (Arbeláez, et. al, 2004).

After an initially slow recovery, Colombian real economic growth rose to 6.8% in 2006. The economic recovery has been reached through a combination of fiscal reform and actions to reduce public debt, policies that substantially reduced inflation, and measures to strengthen the financial system. After seven years of IMF economic programs, Colombia left formal IMF support at the end of 2006. The combined public sector fiscal deficit was reduced from 5.5% of the GDP in 1999 to a projected 0.8% of the GDP in 2007. The gross public debt also declined from 57% of the GDP in 2002 to 45% in 2006. Inflation fell to its lowest level in decades, to about 4.5% in 2006. The economy has showed a sustained growth in exports and a recovery in capital inflows.

The results of the fiscal adjustment program and security and defense strategy have been successful in placing the country on a path of sustainable growth. This stronger growth has been aided by a favorable global economy.

Other Figures for the Country	2006
Population (millions)	46.7
Per capita income (US $)	2,908
Poverty (% of population below national poverty line)	45.1%
% of population in extreme poverty	12.0%
Unemployment rate	11.8%

Source: World Bank and National Statistics Department

Table 1. Some economic indicators

Economic recovery and reforms to strengthen the financial sector. The health of the financial system recovered as loan quality improved and bank profits increased. In 2006, a new financial regulatory agency was formed (Financial Superintendence) by merging the agencies in charge of supervising institutions related to finance and securities. Provisioning levels were brought up to international standards. At the moment, the authorities are developing reforms to, among other things, strengthen creditor rights. The government will also submit a financial reform bill to Congress in 2008 that includes strengthening of the Financial Superintendence as an important goal (see Section 4.1).

Sustained output growth has made it possible to reduce poverty and expand productive capacity. Unemployment declined from 20% in 2000 to about 11.8% in 2006, while poverty fell from 58% of the population in 1999 to 45.1% in 2006 (Table 1). People in extreme poverty also declined from 25% in 1999 to 12% in 2006. However, these figures indicate that reducing unemployment, raising living standards and reducing poverty more substantially remain important policy challenges for the authorities.

Increase in temporary/contract employment. The performance indicators of unemployment could be explained, among other things, by high payroll costs, resulting from permanent fiscal and parafiscal surcharges, and by structural difficulties for low skill job creation.[12] Besides, the quality of jobs being produced in the economy does not contribute toward enhancing welfare. As a result of recession firms hire an important percentage of temporary workers, who enjoy less job security and receive fewer benefits than permanent employees. Underemployment, defined as a situation for the worker that implies that he wants to work more hours, he wishes to find a job that permits him to make better use of his skills, or he wishes to improve his income, is still high and affects at least a quarter of the people holding jobs.

Increase in informal employment. Legal job benefits like a health insurance or savings in retirement funds cover a low proportion of workers. This feature of the Colombian economy is explained by its high level of informality. Using the Schneider and Enste (2000) definition of informality, as lawful activities that do not comply with ordinary legal demands and requirements, it has been estimated that the informal economy represents close to 50% of the GDP.[13]

[12] See World Bank (2002) Colombia Poverty Report.

[13] See Cárdenas, M. and Mejía, C., 2007. Informality in Colombia, New evidence. Working paper N° 35, Fedesarrollo.

The high level of informality is explained by the deep economic crisis at the end of the nineties and by other factors of a structural nature such as the increase in the corporate tax burden, including other labor costs that are different to salaries. The impact on job quality has been important seeing that since the nineties there has been an increase in informal employment in Colombia. In 2002, the percentage of informal workers in relation to the occupied people (informal and contract employment) was 61.3%; for 2005, this percentage was reduced to an even higher level, 58.8%.

Additionally, as has been mentioned, the underemployment that affects an important part of the employed is particularly relevant in the informal sector: 45% of the informal employees classify themselves as underemployed. Besides, the high level of informality is related especially to work in micro-businesses. According to the DANE, 86% of the informal employment was generated in micro-businesses in 2005.

The high unemployment, temporary employment and informality in the Colombian economy must be factors that insurance companies bear in mind when designing Microinsurance products, including premium collecting mechanisms and terms. Particularly, insurers may have to look at coping with flexible incomes of the informal workers and unemployed.

3.1.1. The Colombian financial inclusion priority

Since the early nineties, the provision of credit to micro, small and medium enterprises has been an important part of a policy to promote small business in Colombia. Colombia, as well as many Latin American countries, has been working since the early nineties on the provision of financial services, mainly credit, to small business. This policy has been part of the fundamentals for a wider policy to enhance micro, small and medium enterprises that was implemented in Colombia through the Law 78, 1988, subsequently modified by the Law 590, 2000. The micro credit policy has been developed through MFI-NGOs, some commercial banks and financial cooperatives.

The developing of microfinance in Colombia does not differ from that of other countries in the region. During the nineties two approaches for the provision of financial services to small business and low-income people were consolidated in Latin America: the MFI-NGO and commercial banks entering in micro credit. They both have market criteria, and according to Marulanda y Otero (2005) this model will prevail in the region in the next decade with particular features. On the one hand, the MFI –NGOs will undergo "upscaling" to become regulated entities in many countries, while on the other hand, commercial banks will enter a "downscaling" process to provide a range of financial services to the poor.

Particularly, in Colombia the upscaling process of MFI has only been debated but without any specific decision on that matter. In contrast, the downscaling process has led to an important increase in micro credit provided by commercial banks and financial cooperatives. Particularly, microcredit provided by private banks has increased from US$69 millions in 2002 to almost US$398 millions in 2007 (Table 2 below). This trend has been reinforced by the financial inclusion policy which has been implemented since 2006 through the Opportunity Bank Program. As we will see farther on, this program is focused not only on credit but on other financial services, including insurance, to both low income people and small business.

Loan Portfolio
US$ Millions

Year	Total	Total Microcredit	Provided by: Financial Cooperatives supervised by FS	Private Banks	Government Banks 1/
2002	16.297	137	1	69	37
2003	17.783	205	1	103	101
2004	23.523	353	1	162	130
2005	28.611	550	2	224	324
2006	38.723	752	6	295	451
2007	54.160	982	10	398	575

1/ This is the Agricultura Bank owned by the government.
Source: Financial Superintendence data.

Table 2. Loan portfolio in Colombia

There are two main reasons that explain the downscaling process. First, the consolidation of the Micro Finance industry by the end of the nineties showed that MFIs could be profitable, financially self-sustainable, serving the low income people without higher risk. Second, competition resulting of the financial liberalization undertaken in the early nineties led commercial banks to seek for new market niches. Competition was increased as a result of the reforms that opened the financial systems to foreign investment, the decline of inflation and the reduction of margins (interest rate spreads) in the traditional segments of the market. Although spreads did not decrease as was expected in Colombia, for different reasons such as a lack of efficiency and high non financial costs, Barajas *et al.*(1999) find evidence of increased competition in banking.

<u>Enhance access to financial services: a fundamental part of the poverty reduction policy issued in 2006.</u> There are numerous references in economic literature to the importance of broad financial services and access of poor people to them. This literature brings out the relationship between finance and growth and, particularly, the importance of a well-developed financial system and the access of low income people to it for economic development and poverty alleviation.[14] This view is an important fundamental of the Colombian government policy to reduce poverty and improve equity.

Access to financial services is very low in Colombia. According to a study made in Bogotá in 2003, only 40% of the population has some kind of access to financial services. The study concludes that this percentage could be considerably lower if it were extended to the entire country.[15] In the same way, an analysis of the bank usage level executed for the Ministry of Finance found that only 28% of the families have a savings account, the financial product that is used most in Colombia. In said analysis, the percentage of bank usage per income level is barely 20% for the lower income group, while it exceeds 80% in the higher income group[16].

[14] See Beck, Demirguc-Kunt and Levine (2004).

[15] See Solo and Manroth (2006).

[16] See Marulanda Consultores (2004).

ASOBANCARIA, the association of banks and other credit entities, estimated for March 2007 that 33.6% of the population has access to some type of financial service.

Box 1. Socioeconomic Strata

In Colombia the tool most often used to classify the population according to income is socioeconomic stratification. This tool classifies the people from the different municipalities of the country into different strata or socioeconomic groups, according to the characteristics of their housing and surroundings. Although this stratification is undertaken mainly for the purpose of charging differential rates and assigning subsidies for residential public utilities, it has also been used to orient the planning of public investment and the development of social programs in the zones where they are most needed. Thus, it is used as an indicator of people's socioeconomic situation. The stratification operates on a scale from 1 (greater needs) to 6 (fewer needs).

The relationship between income brackets and strata shows that there is a high concentration of the Colombian population (43%) living in homes located in stratum 3, followed in importance by the percentage of people living in stratum 2 (34%). Although strata 2 and 3 include people from all income brackets, the majority of the people in income brackets 1 and 2 live in homes located in strata 1, 2, and 3.

Percentage of the population per income bracket

Income bracket	Strata					
	1	**2**	**3**	**4**	**5**	**6**
1	13	50	32	3	1	1
2	12	56	31	1	0	0
3	9	47	39	3	1	0
4	5	38	49	6	2	1
5	2	13	48	21	9	7
Total	6	**34**	**43**	10	4	3

Source: DANE, Quality of Life Survey 2003.

The Opportunity Bank Policy. In this context, the government has identified microfinances as a fundamental factor in its poverty reduction policy and to enhance equity. But with the fostering of microfinance the government is also promoting a higher level of bancarization especially among poor people. The government is seeking a higher use of the formal financial sector in low income people not only through credit and savings, but also as a channel to strengthen payments systems and a way to access insurance products.

Particularly, the government view on insurance products is in tune with the social policy approach focused on social risks management rather than on the social protection approach that mainly seeks to support people.[17] Low income households face risks that produce poverty temporarily, and families do not have the mechanisms to handle them. In that sense access to financial services is a central goal in a policy of social insurance to reduce poverty.

[17] See Holzman (2003). The World Bank's approach to social protection in a globalizing world.

The micro finance policy called Opportunity Bank policy (La Banca de las Oportunidades in Spanish) is based on an investment program created in September, 2006. The program aims to enhance access to financial services, particularly for low income households, in order to promote development of social equity. The program aims to provide essential financial services to low income people (which includes payments and transfers, savings, loans, insurance and pensions and remittances) and is supported by a network made up of banks, commercial finance companies, NGOs specialized in micro credit, financial cooperatives and Family Benefit Funds. This policy will be an important driver to strengthen microinsurance supply in Colombia. However, until now, policy development has been focused mainly on credit.

The number of persons that has access to these services for the first time is increasing due to the broad-based strategy that the financial system has been adopting in the scope of the policy of the Banca de las Oportunidades. In effect, according to ASOBANCARIA, between 2006 and 2007 close to a million Colombians became linked to formal credit via the different alternatives the market is offering. As part of the Banca de las Oportunidades policy, in 2006 the regulation created the non banking correspondants form to offer financial services in poor neighborhoods and remote places. At June 2007 there are 3,508 non banking agents in operation. Banca de las Oportunidades and its impact on the insurance sector is discussed in more detail in Section 4.1.5.

Credit life insurance: a first approach to insurance products for low income people. The growing of micro credit provided by commercial banks in Colombia promoted the usage of credit life insurance between micro credit clients. Though, some analysts think that in many cases micro credit clients do not even know that they have this kind of insurance which is more in the interest of the bank, for others this is a first approach to an insurance product by low income clients and they learn that it works when there is a claim. In fact, many insurance companies in Colombia entering into microinsurance have used that first contact with micro credit clients to offer other life and non life products more suitable to the needs of low income people.

Credit life insurance is a mandatory practice for credit institutions in Colombia. Particularly, Art. 101 EOSF establishes that credit institutions must insure immovables or real state that belong to them or that guaranty mortgage-related credits. Besides, banks could include a credit life insurance as part of the credit contract in other types of credits. In fact, some MFI-NGOs that are not supervised by FS use credit life insurance linked to the micro credit.

3.2. Colombian Insurance Industry

The insurance sector's assets (life and non-life companies) were 5% of GDP in 2006. However, traditionally the banking sector has been larger than the non-banking sector in Colombia. The banking sector's assets, including all credit institutions, were almost 49% of GDP in 2006. The assets of the private pension funds were close to 13.5% of the GDP in 2006 (Table 3).

Colombian Financial System: Assets 2006

Institutions	US$ Millions	% of GDP
Credit institutions	66,119	48.6%
Banks 1/	58,058	42.7%
Corporaciones Financieras	1,555	1.1%
Compañías de Financiamiento Comercial	6,182	4.5%
Financial Cooperatives	324	0.2%
Insurance companies	**6,886**	**5.1%**
Life	3,372	2.5%
Non Life	2,776	2.0%
Insurance Cooperatives	106	0.1%
Sociedades de capitalización	633	0.5%
Pension Funds	18,379	13.5%

1/ Includes private and public banks and excludes second-tier development banks

Source: Financial Superintendence and DANE.

Table 3. Colombian financial system assets, 2006.

The insurance market is formed mainly by 43 insurance entities; 41 are corporations (one is the state-owned corporation Previsora) and 2 are cooperatives (Solidaria and Equidad). Besides, in the market there are 26 reinsurance registering entities (10 Reinsurers' Offices and 16 Reinsurance Brokers), 46 independent insurance brokering entities, insurance agents, and adjusters**.**

Over the past three years Colombia's insurance industry has been showing an important growth and in 2006 life insurance grew more than non-life insurance. This take-off is due mainly to the fact that industry has started playing a more active role after the economic crisis of late nineties (Table 4). In spite of the significant growth exhibited by the Colombian Insurance Market in the last three years, the country presents a moderate insurance penetration and a low insurance density. The premium, as a % of GDP is 2.4 % (Latin American and Caribbean average is 2.4%) and the premium per capita is only US$ 69.1 (Latin American and Caribbean average is US$ 126.7)

Colombia's Premium Volume (in millions of US$)

	Life Premium	Nominal Change (in %)	Non-Life Premium	Nominal Change (in %)	Total Premium	Nominal Change (in %)
2001	496		1,463		1,959	
2002	548	10.5%	1,577	7.8%	2,127	8.3%
2003	550	0.4%	1,443	-0.1%	1,990	-6.1%
2004	645	17.3%	1,691	16.7%	2,336	16.9%
2005	761	18.0%	2,005	18.6%	2,767	18.5%
2006	947	24.4%	2,253	12.3%	3,200	15.6%

Source: data extracted from Sigma N°4/2007, N°5/2006, N°2/2005, N° 3/2004 N°8/2003; Swiss Re.

Table 4. Insurance premium volumes in Colombia.

The principle branches of the market are "Vehicle" insurance and "Life Group and Collective" life insurance followed by "Fire and Earthquake" insurance, "Transit Accident Compulsory Insurance, TACI" and "Health" (Table 5). (See details in Appendix 2 and 3 on Portfolio Composition).

Main Insurance Portfolio
(US$ Millions)

	Written Premium 2006	% of Share
Life Group and Collective	364	11,4%
Health	157	4,9%
Vehicle	575	17,9%
Fire and Earthquake	271	8,5%
TACI	198	6,2%
Others	1,639	51,2%
Total Market	3,204	100,0%

Source: data extracted from official website of Financial Superintendence.
Exchange Rate: 2005: US$1 = Colombian $2,320,8; 2006: US$1 = Colombian $2 358,0
TACI: Transit Accident Compulsory Insurance

Table 5. Shares of different types of insurance in premiums.

Table 6 shows the lack of development of insurance particularly in life insurance. According to opinions picked up in the market, the low level of life insurance in Colombia has several sources. One of these lies in that the people of higher income groups buy their insurance outside the country, due mainly to the fact that the regulation does not forbid foreign entities from offering insurance within Colombian territory. There is also a low insurance culture.[18]

	Premium % GDP		Premium Per Capita US$	
	Life	Non-Life	Life	Non-Life
2005	0,62	1,61	16,8	43,6
2006	0,70	1,70	20,5	48,7

Source: Sigma N°4/2007 and N° 5/2006, Swiss Re.

Table 6. Insurance premiums as % of GDP and per capita in Colombia.

In relation to the solvency of the market, the current regulation requires insurance companies to maintain their total technical reserves backed with admitted investments. At aggregate level, the market complies with this requirement. By March, 2007 it exhibited an excess of investments for US$ 376 million (Table 7).

US $ millions	Non Life	Life	Total
Investment	1,623	2,904	4,527
Technical Reserves	1,611	2,540	4,151
Excess of Investment	12	364	376
Equity	967	1,002	1,969
Minimum Capital	602	543	1,145
Solvency Margin	271	261	532
Excess of Minimum Capital	331	282	613

Source: data extracted from official webside of Financial Superintendence.
Exchange Rates: US$ 1 = Colombia Pesos 2,155.06, TCRM.

Table 7. Reserves and Equity Insurance Sector, March 2007

[18] See Junguito, R. (2007) and Martinez *et al.* (2007) on the importance of insurance culture for Colombia.

In relation to equity requirements, all the insurance companies have the Minimum Capital and the Solvency Margin required by the regulation. We can observe an excess of Minimum Capital equal to US$ 613 million. We must point out that the current regulation indicates that insurance companies are free to invest their equity and other funds that do not belong to the technical reserves. The insurance sector complies with the solvency requirements demanded by current regulations.

Another aspect to be pointed out in the Colombian insurance market is the high concentration of life insurance sales in two companies that concentrate almost 40.4% of the business. In non-life insurance the concentration is softer. Only two companies concentrate 21.3% of market (Appendices 4 and 5).

4. Regulatory Analysis

In contrast to the majority of the insurance markets, the Colombian insurance market is not ruled by an exclusive Insurance Law. Current financial regulation in Colombia is based on the type of entity rather than on the activities that they perform. The insurance activity, together with other financial activities, is regulated in the Fundamental Law of the Financial System (FLFS), in Spanish Estatuto Orgánico del Sistema Financiero (EOSF).[19] The FLFS is a compilation of the main financial laws, which consists of different legal and administrative norms of a general nature derived from a fundamental Law. The FLFS governs the functioning of both the financial sector and the insurance sector.

To date there is no dedicated regulatory framework for Microinsurance despite many insurance companies in Colombia providing products to low income people. In fact, there is also no broad Micro Finance definition in Colombian legislation like there is in many countries. Micro finance matters focus mainly on micro credit as a development tool. In this sense, the Law 590, 2000 seeks to promote the development of micro, small and medium enterprises and considers micro credit as one of the development factors. Article 2 of Law 590, 2000 defines micro enterprise by size indicators through a combination of number of employees and assets. In Article 39 the law defines micro credit systems and again this definition is based on a maximum amount of credit (25 current monthly legal wages), that, for 2007, is close to US$5.400 for each debtor.

During 2007, however, the Colombian government was working on a bill that will reform the financial sector Law (FLFS). The Financial Reform Bill was submitted to Congress in April, 2008. Though the draft includes topics related to the promotion of access to financial services, it is mainly focused on consumer protection, banking services, and investment of pension funds resources.

The FLFS defines as insurance entities: insurance companies, insurance cooperatives and reinsurance companies. There are two insurance companies belonging to the cooperative sector. All insurance entities are supervised by the Financial Superintendence. In addition, there are contractual savings companies – in Spanish called Capitalization Companies - that

[19] Decree 663 of 1993.

are separate from insurance companies and pension funds, and in some cases sell life insurance combined with saving securities (Art. 4 FLSF). These Capitalization Companies, supervised by the Financial Superintendence, offer saving securities with a short term defined as a form of contractual savings, suitable for people with low saving capacity. Legislation separates them from other contractual saving entities like insurance companies and pension funds. Savings in those contractual companies are lower than life insurance premiums because it is a product that has fallen into disuse, but at the moment the Government is interested in enhancing access to this type of savings products in order to enlarge saving options for low income people. Besides, there are also funeral entities that offer a kind of funeral insurance but are unsupervised (see Section 5.1.1).

The FLFS governs both insurers and intermediaries, as well as contractual savings companies already mentioned, and reinsurance companies. However there are also entities other than regulated insurance intermediaries that play an important role in the distribution of insurance products such as funeral entities, financial cooperatives and family benefit funds, among others. It is important to note that the latter are distribution channels in an economic sense, and in practice, normally operate under collective insurance schemes, so it is the insurance company that will be responsible before the client.

In this section an analysis will be made of the current insurance regulation, which entails a revision of laws and decrees related to life and non-life insurance. An analysis will also be made of the instructions issued by the Financial Superintendence of Colombia known as "resolutions", "external circulars" and "circulars letters". Others laws, decrees and instructions related to insurance and that originate in other supervisory and regulating entities will also be reviewed.

4.1. Overview of the current regulation relevant to insurance as well as changes currently underway

*The Fundamental Law of Financial System (FLFS)***,** *Decree 663, 1993*, is the main regulatory body that applies to the insurance market. It defines financial institutions under the supervision of the Financial Superintendence as being comprised of: i) credit institutions (banks, finance corporations that are investment banks, commercial finance companies that are focused on consumer credits, and financial cooperatives); ii) financial service companies (fiduciaries and pension funds, among others); iii) <u>insurance companies and insurance and reinsurance brokers</u>.

Until the beginning of the 90's the Colombian financial sector operated under a scheme of specialized banking. This system was characterized by: i) specialized entities created for different financial objectives and with specific authorized activities; ii) isolation between different financial system instruments, and iii) severe investment restrictions for deposit-taking institutions in the real sector.[20]

[20] De la Cruz, J. and Stephanou, C. (2006).

At the beginning of the 90's law 45/1990 adopted a "multi-banking" system (introducing the concept of matrix-subsidiaries) that permitted equity participations between some financial institutions. In contrast with the specialized banking scheme, this reform promoted the creation of financial conglomerates. Besides, the sector was open to foreign investment through this law. In the insurance sector foreign ownership has increased in life and non-life activities. Currently more than 40% of insurance company's equity belongs to foreigners.[21]

The structure of the Fundamental Law of Financial System is presented below (Box 2). The FLFS is divided into thirteen parts (Appendix 8). Only sections one, two, three, six, seven, eleven, twelve and thirteen are relevant for the insurance sector. The first, third and sixth part of the FLFS are the most important from the point of view of this study, because they establish operating bases of the insurance activity.

Box 2. Structure of the Fundamental Law of Financial System

- **First** Part "Basic description of the entities submitted to the supervision of the Financial Superintendence"

  This part contains thirteen chapters and four of them are linked with insurance.

- **Second** Part "Intervention in the Financial and Insurance activities"

  Unique Chapter Establishes the receivership functions of the National Government as regards financial and insurance entities.

- **Third** Part "Financial Institutions operations norms"

  This part contains twenty-one chapters and all of them are in one or another form linked with insurance.

- **Sixth** Part "Conditions of the Capitalization activity and operations of insurance companies, reinsurances and Insurance intermediaries"

  This part contains seven chapters and all of them are linked with insurance.

- **Seventh** Part "Sanction System: System applicable to the insurance companies and to the directors, managers, legal representatives, and fiscal ticket inspectors or other officials of the companies"

  This part contains four chapters and all of them are linked with insurance.

- **Eleventh** Part "Procedure for the possession and Liquidation of the entities submitted to control of the Financial Superintendence"

  This part contains three chapters and all of them are linked with insurance.

- **Twelfth** Part "Procedure for selling of State-owned shares in Financial Institutions and Insurance Entities"

  This part contains three chapters and all of them are linked with insurance.

- **Thirteenth** Part "Inspection and overseeing authorities"

  This part contains two chapters and all of them are linked with insurance.

[21] Junguito, R. (2007)

The Colombian market is governed by other important regulations that complement the FLFS (Figure 2) and that are presented below.

REGULATION ON INSURANCE ACTIVITY

	Regulations that complement the FLFS	
The Fundamental Law of the Financial System FLFS (Decree 663,1993) regulates all financial activities,including insurance activity.	The Comercial Code	Regulation on the insurance contract and the brokerage
	External Circular 100,1995	Establishes rules on financial and accounting matters.
	External Circular 007,1996	Establishes rules on legal matters as minimum capital, investment rules and consumer protection, among others
	Resolution 1063, 1998	Credit risks, securities rating agencies and investment grade
	Resolution 8, 2000	Authorize life Insurance product sales in dollars
	Decree 094, 2000	Insurance companies investment rules
	Decree 2779, 2001	Investment rules of technical reserves
	Decree 690, 2003	Regulation on consumer protection
	Regulation on intermediaries	
	Decree 361, 1972	Regulation on insurance brokers activity.
	Decree 2605, 1993	Rules on insurance intermediaries and supervision matters.
	Law 389, 1997	Modifies the Commercial Code on insurance contract and introduce bancassurance
	Decree 1367, 1998	Define insurance branches to be sold through *bancassurance*
	Law 510, 1999	Modifies the FLFS on insurance intermediation
	Law 795, 2003	Modifies the FLFS and precises funeral entities role
Other regulation related with micro insurance	Law 527, 1999	Regulation on e-commerce
	Decree 1400, 2005	Regulation of payment systems (credit and debit cards)
	Law 590, 2000	Promotes micro and small business and define micro credit
	Decree 3078, 2006	Creates Banca de las Oportunidades Investment Program
	Decree 2233, 2006	Creates non banking correspondents
	Decree 828, 2007	Clarifies charges authorized to public utilities invoices
Regulation on Cooperative sector	Law 79, 1988	Modernizes legal rules to cooperatives
	Law 454, 1998	Strength regulation on solidarity economy sector

Figure 2. Regulatory scheme

Cooperative Activities and Solidarity Economy Sector Law

Law 79, 1988 on Cooperatives. In 1988 the Colombian government modernized legal rules related to cooperatives, through Law 79, 1988. This law established a new framework to develop cooperative activities in Colombia that is in force up to date. The main reforms included in the law were: i) to distinguish between associate (member) condition from worker condition in a cooperative, in this manner a cooperative associate could not work in a cooperative activity; and, ii) to include non associates as beneficiaries of the cooperative activities, thus non associates can be benefited by cooperative services. These are specific features of the Colombian cooperative legislation.

According to article 4, a cooperative is a non-profit organization, whose members and workers are simultaneously the contributors and promoters of the organization. In addition, the law establishes that a cooperative will be created to jointly and efficiently produce or distribute goods and services, in order to satisfy the needs of members and community in general.

This law defines insurance cooperatives as specialized cooperatives (Art. 72) and establishes that these must submit to the surveillance of the Financial Superintendence (Art.99 and Art 151).

Law 454, 1998 on regulation of solidarity economy sector. As a result of the financial crisis at the end of the nineties, a law was issued to strengthen regulation on the solidarity economy sector. Law 454, 1998 specified a framework to regulate the solidarity economy, created the Superintendence of Solidarity Economy and the Guaranty Fund of Financial Cooperatives, enhancing and deepening Law 79 of 1988. In particular, Law 454, 1998 established rules on financial and insurance activities fulfilled by cooperatives. This norm also demands that insurance activities fulfilled by cooperatives must be carried out by insurance cooperatives as entities specializing in such activities (number 3 Art 39).

Agreeing with these rules, the FLFS establishes that the cooperative agencies that provide insurance services must be specialized, supervised by the Financial Superintendence, and carry out the insuring activity especially in the interest of its own associates and of the community linked to them (number 5, article 38 FLFS). The FLFS establishes that any foresight service offered by a cooperative to its members, which could be assimilated to an insurance product must be sold by a legally formed insurance company or insurance cooperative. If such insurance entities are legally formed, they must be supervised by the Financial Superintendence.

Box 2. The Solidarity Economy Sector

Colombia has a wide-ranging solidarity sector formed by non-profit legal entities. A broad sector of the solidarity economy is composed by organizations such as cooperatives, mutual associations and employee funds. In general, the workers or the associates (members) in these entities, as the case may be, are doing the contributing and managing simultaneously. Particularly, in Colombia cooperatives play an important role in financial activities specially serving people with low saving capacity and limited access to credit.

The cooperative sector is composed of cooperatives authorized to carry out financial activities and cooperatives that fulfill non-financial activities. Traditionally, the former category has offered financial services to low income people and people in far regions that cannot regularly access formal financial institutions like banks. In 1988 the Colombian government modernized legal rules to cooperatives, through Law 79/1988. This law established a framework to develop cooperative activities in Colombia that is in force to date. The main reforms included in the law were: i) to differ associate (member) condition from worker condition in a cooperative, in this manner a cooperative member could not work in the cooperative; and, ii) to include the non associate community as beneficiaries of the cooperative activities, thus non associates can be benefited by cooperative services. These are specific features of the Colombian cooperative legislation.

Table 8 shows the types of cooperatives that carry out financial activities and their supervision authority. In this group, financial cooperatives and insurance cooperatives are supervised by the Financial Superintendence because they provide financial services to associates and non associates.

Cooperatives fulfilling financial activities	Number	Provide financial services to	Supervised by
Financial Cooperatives	6	Associates and non associates	Financial Superintendence
Cooperatives of saving and credit	209	Only associates	Superintendence of Solidarity Economy
Cooperatives with a saving and credit section		Only associates	Superintendence of Solidarity Economy
Cooperative Insurance	2	Associates and non associates	Financial Superintendence

Companies			

Table 8. Overview of cooperatives in Colombia.

According to Article 95 of Law 795 of 2003, which reformed some aspects of the FLSF, financial cooperatives can carry out real-estate micro-credit operations that are oriented toward income brackets 1 and 2 (see Box 1).

The financial crisis of the late nineties also had a negative effect on financial cooperatives and led to the closing of some bank cooperatives. However, users of cooperative financial services maintained their trust and the Government strengthened regulation and supervision legislation on the solidarity economy sector. In fact, Law 454/1998 specified a framework to regulate the solidarity economy, created the Superintendence of Solidarity Economy and the Guaranty Fund to Financial Cooperatives, and established rules on financial activities fulfilled by cooperatives. With stronger regulation and supervision, the important role of financial cooperatives remained in spite of the crisis.

The consolidated figures and forecast to the closing of 2006, delivered by Confecoop (the association of solidarity economy entities), give a total of 8,970 entities of the solidarity economy sector, of which 6,877 are cooperatives; 1,866 employee funds and 227 mutuals (Table 9). The employee funds provide savings and credit services to their members in accordance to their capacity to save and their needs.

THE SOLIDARITY ECONOMY, 2006

Entities	Number	Workers	Members	Assets (US $)
Cooperatives	6,877	114,924	3,682,496	6,928,856,500
Employee funds	1,866	7,843	677,248	1,479,208,500
Mutuals	227	2,971	146,419	154,553,500
Total	8,970	125,738	4,506,163	8,562,618,500

Source: Confecoop, 2006.

Table 9. Overview of the solidarity economy

At December 2006, cooperatives grouped 3,682,496 associates. Furthermore, the members of the employee funds amount to 677,000 and the mutual associations have 146,000 members. Almost 62% of cooperatives are micro enterprises and 29% small enterprises, accordingly assets size definition used in Colombia (Law 590, 2000). On average, small cooperatives have 67 associates, micro cooperatives have 354, medium cooperatives have 1,357 and big cooperatives have 13,948.

In addition to financial services, cooperatives carry out activities on health, education, agricultural, transport, funeral services, and associate work, among others

The insurance cooperatives currently operate in life and non-life insurance. There are two insurance cooperatives, La Equidad is an insurance cooperative formed by 2 insurers La Equidad Property and La Equidad Life and their owners are more than 1,200 agencies of the Colombian Solidarity Economy.

Aseguradora Solidaria, the other insurance cooperative, belongs to different cooperatives that, in the past, have usually supplied funeral services in different regions of the country. Since 2004 the main owner is_the National_Funeral Network Los Olivos (the biggest funeral service network of Colombia).

La Equidad and Solidaria issue insurance policies to associates and non associates, but their target maket are persons and institutions in the solidarity sector. They don't have any restrictions as regards issuing or selling policies to persons or institutions that are not part of the solidarity sector, but their strategy is to focus on the solidarity sector as their natural market. As was mentioned above, taking into consideration that La Equidad and Solidaria issue insurance policies to third persons or non associates, they must be supervised by the Financial Superintendence as all insurance companies in the market are.

The Financial Reform Bill. A financial reform bill was submitted to Congress in April, 2008. The bill covers five main areas: i) Financial sector structure; ii) Topics related with pension funds operation; iii) trade liberalization of the insurance services; iv) promotion of access to financial services for low income people, particularly banking services; and v) strengthening of the Financial Superintendence and consumer protection. The main aspects of the reform that could have an impact on the insurance sector are the opening of cross-border trade in insurance and the removal of certain market access conditions related with right of establishment.

With regard to cross-border trade in insurance, Colombia has a restrictive cross-border trade regime for insurance. The bill contains some changes in the market seeking greater competition for insurance companies established in the country.

Notwithstanding that at present all financial institutions established in Colombia could be of foreign ownership without any limitations, there are certain market access restrictions. Particularly, foreign banks and reinsurers can offer their services in Colombia without having to constitute a subsidiary, but only a representative office. However, it is impossible to have commercial presence in Colombia through direct branching and offer financial services domestically. Foreign insurance entities cannot operate and sell insurance directly in Colombia (Art. 39, 108 y 188 FLFS); to do so they must set up a subsidiary in the country in accordance with the provisions of the Constitution and the law. Thus, the insurance activities must be capitalized in Colombia and subject themselves to Colombian regulation. Access of foreign financial institutions implies organizing them as legal entities under Colombian laws and with legal forms in which such entities could be set up in Colombian financial legislation. Sanctions are established in Articles 209 and 211 of the FLFS. In particular, the reform seeks to allow the establishment of insurance companies in Colombia as branches.

The market access section of the bill is currently only focused on promoting access to banking services for the poor. Insurance companies are seeking that government study the insurance marketing scheme as part of enhancing access to financial services, in order to fit it into the characteristics of microinsurance products. Fasecolda, the association of insurance companies, has tackled some questions that must be analyzed within this reform process.[22] The questions relate to whether microinsurance must be a special branch in insurance activity, policies must have formal standard conditions and policy prices must be regulated, among others. At the moment several meetings to discuss these matters have been held between insurance companies, government officers and congressmen.

[22] The Federation of Colombian Insurers, Fasecolda, is the Colombian Association of Insurance Companies. Fasecolda is a domestic association, with foreign and national members and groups all insurance companies located in Colombia disregarding the precedence of its equity. This association carries out permanent activities for the development of the sector, both in the national and international ambience.

4.1.1. Institutional and prudential regulation on insurance and reinsurance companies

The review of the regulation considers the following topics: licensing**,** solvency margin, technical reserves, investments, risk control, reinsurers, market conduct (market insurance policies, intermediation and consumer protection), corporate government, risk rating, outsourcing of administrative functions, financial services as well as the self-regulation code adopted by the industry. The availability of new technologies will also be analyzed as the target is to introduce broad-based products in the insurance market.

Regulation on Licensing. To operate and form an insurance entity in Colombia, an authorization of the Financial Supervision must be obtained. Interested companies must be legally established in Colombia in compliance with FLFS provisions (Chapter I, Part Three) and External Circular 007, 1996 (Number 1, Chapter One, Section I), that contain the procedure that must be followed to request the formation of an insurance entity. Principal requisites are:

i) Legal Form. Insurance companies located in Colombia have to be constituted in the form of stock companies or cooperatives. In relation to insurance draft the FLFS does not include a definition on the insurance business and neither has it defined life insurance companies and non-life insurance companies. When the Superintendence authorizes an insurance company to operate in Colombia, it authorizes, at the same time, in which branches it will operate (by request of the interested parties).

ii) Minimum Capital: The minimum capital is determined by the "Minimum Capital for Incorporation" (basic capital) plus the "Capital by branches". The minimum capital is regulated and has to be adjusted yearly. The Minimum Capital for Incorporation (2006) for insurers (life and non-life) is US $ 2.7 mill. (Colombian $ 6,480 mill) for credit and export insurers it is US $ 1.5 mill. (Colombian $ 3,447 mill.) and for reinsurers it is US $ 11 mill. (Colombian $ 25,916 mill.). Table 10 presents the "Capital by branches" established in 2006 by business line.

Business Line	Technical Equity US $ millions	Business Line	Technical Equity US $ millions
Vehicles	0.9	Disability and Survival	0.5
Export Credit	0.7	Pensions Law 100	1.2
Transit Accident Compulsory Insurance	0.6	Voluntary Pensions	0.9
Fire, Earthquake and Loss of Revenue	0.6	Worker Compensation	0.8
Guaranty (Surety)	0.6	Disease of high cost	0.5
Transport	0.3	Life Groups	0.5
Individual Life	0.5	Others Insurances Risks	0.3

Exchange Rate:US$ 1= Colombia $ 2,358 (2006)

Source: Financial Superintendence.

Table 10. Capital by branches, 2006

Special requests of "Capital branches" and "Solvency Margin" for the microinsurance are not demanded. The microinsurance is considered in the risk class that corresponds in accordance with its coverage. The regulation needed on capital has not restrained the development of microinsurance, because the insurance companies have incorporated these products as part of their business as a whole.

Solvency Margin. In addition to the “Minimum Capital” the regulation requires insurers in operation, to mantain a “Solvency Margin”. (Art. 82, Nº 2 FLFS and Nº 2.1.1, Chapter 2, Section Six of Circular 007, 1996).

The procedure to estimate the Solvency Margin is determined for non-life and individual life insurances, professional risks companies and cooperatives. The formula and factors are established by the regulation; they are of general application for all insurers. The regulation does not demand that the equity or part of the equity be invested in accordance with an established regime. The instructions point out expressly that insurance companies are free to invest their equity and other funds that are not part of the technical reserves (Art. 182, Nº2, FLFS).

Insurance entities whose object is the practice of individual life insurance must be dedicated exclusively to this field, without spreading their activity to another class of insurance operation unless they complement each other. (Art.38 FLFS) This means that the life companies apart from the “individual life insurance” can sell: life group, health, personal accident, education, voluntary annuities, disease of high cost, funerals, annuities and life collective (See Appendix 2)

Except for “individual life insurance”, the non-life insurance companies may operate the branches of “collective life” and “health” insurance. This means that the non-life companies in addition to the traditional property and casualty insurances can sell “collective life”, “life group” and “health” insurance (see Appendix 3)

iii) Main documents about the nature, responsibility and suitability of the investors. The main information that the regulation requires from the shareholders, Board members and executives seeks to provide the market with persons who are qualified morally and professionally. The regulation also requires knowing the source and origin of the resources, and the investments that the investors have, directly or indirectly, in the financial sector. Also required is a business plan that demonstrates the viability of the insurance company to be established, and a five-year projection of the entity.

Funeral entities. In Colombia there are funeral companies offering funeral services, which are not insurance companies and are unregulated from an insurance point of view. The insurance industry considers services provided by these entities as funeral insurance provided without an insurance license and therefore consider them unauthorized entities that do insurance business. Nevertheless, Article 111 of Law 795, 2003 pointed out that the funeral services do not constitute an insurance business because this is a legal relationship that “does not constitute an insurance contract”.[23]

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[23] Insurance contract definition: Legally binding unilateral agreement between an “insured” and an “insurance company” to indemnify the buyer of a contract under specified circumstances. In exchange for premium payment(s) the company covers stipulated perils” (Barron’s Business Guide, Dictionary of Insurance Terms, Third Edition, Haevey W. Rubin, Ph.D.,CLU,CPCU).

Technical Reserves. Insurance entities established in Colombia must set up: i) Unearned Premium Reserve; ii) Mathematical Reserve; iii) Claims Reserve which include reported and unreported losses; and iv) Deviation Claim Reserve, to meet obligations for not well-known loss ratios and highly fluctuating, cyclical or catastrophic risk. (Art. 186 FLFS). The regulation establishes the technical reserves necessary for the insurance activity and these are applicable to the technical reserves that must be constituted by the responsibility that comes from the micronsurances.

Investments. Technical reserves of insurance companies must be permanently invested exclusively in the assets that the regulation indicates (Art. 182 FLFS, Decree 094, 2000 and Decree 2779, 2001). The insurance companies are authorized to invest up to 30 % of these technical reserves in foreign assets. In order to minimize and diversify the financial risks of the technical reserve investments, the regulation established an investment scheme based mainly on the application of maximum limits. Limits have been established for type of instrument, by issued investment, by business group, among others. The financial instruments must be provided with a risk rating granted by a Risk Agency. The regulation also established that insurance companies can carry out operations with derivatives, but only for protecting fluctuations of interest rates, change of currency or change of share prices. The investments must be valued to "fair value", in accordance with what is established in External Circular 100, 1995. The investment regulation includes simple saving instruments for backing the microinsurance 's technical reserves and derivatives are admitted only for limiting the risks.

Risk Management. The current regulation demands that insurers carry out a control of the essential risks related to the insurance activity. The system considers credit risk, market risk, liquidity risk and underwriting risk. To this end the insurance companies must design and adopt a proper system that allows them to carry out a suitable management of the risks inherent in their activity, known as the "Special System of Insurance Risks Administration" (SEARS in Spanish), (Chapter 5, Section Six of Circular 007, 1996). After the financial crisis of the end of the nineties, financial institutions, including insurance companies, could do their own risk evaluation and the FS has issued different rules to manage all types of risk mentioned.

Reinsurers. Foreign reinsurers and the foreign reinsurer's brokers that meet the following main requirements are allowed to execute reinsurance operations in Colombia:

- Registration with the Financial Superintendence (Reinsurers Registry)
- Reinsurers, classified according to an international risk rating agency (Standard &Poor, A.M. Best, Fitch Duff and Phelps and Moody's) at least in the risk category BBB or other equivalent to it.
- To initiate their activities, Reinsurance Brokers need a registration certificate granted by the Financial Superintendence. A fidelity and financial risk policy and a general civil liability policy are also required.
- Freedom to celebrate reinsurance contracts.

- There is freedom to celebrate reinsurance contracts with the reinsurers recorded in the Financial Superintendence Registry.

4.1.2. Regulation on insurance intermediaries and other marketing channels

In Colombia there are distribution channels for insurance products that are different from the traditional insurance intermediaries: brokers, agents and agencies. As is the case in the rest of Latin America the Colombian insurance market is also dominated by brokers and agents. Nevertheless competition of other marketing channels has arisen (bancassurance, utilities, cooperatives and NGO's). In this section, the regulation for these distribution channels is also reviewed.

Applying the marketing channels defined by Swiss Re to the Colombian market, the Colombian scheme is shown in Table 11.

	Marketing Channels	
Traditional	**Direct**	**New Channels**
▪ Brokers	▪ Telemarketing	▪ Cooperatives
▪ Agents	▪ Mailing	▪ NGO's
▪ Agencies	▪ Internet (*)	▪ Utilities
	▪ Employers	▪ Banks (bancassurance)
(*) Use to back up sales efforts		

Source: Elaborated by the authors based on Swiss Re (2002) Sigma N° 2.

Table 11. Marketing channels in Colombia

4.1.2.1. Traditional marketing channels

In Colombia insurance may be underwritten directly with the insurance company, through agents, insurance agencies or by means of insurance brokers. The activity of insurance intermediaries does not prohibit insurances entities from accepting risks directly without the intervention of the intermediaries (Art. 5 FLFS and Art 2º Decree 2605, 1993*)*.[24]

The level of commissions for brokers, agents and agencies is not restricted by regulation but paying commissions for the work of intermediation to other persons who are not brokers, agents and agencies (Art.188 FLFS) is forbidden. The level of commissions, the forms of payment and other conditions are agreed between the intermediaries and companies.

The brokers, agencies and agents cannot pay claims on behalf of the insurance company and only the agencies can collect premiums.

[24] The Colombian scheme does not differ from other Latin American countries. In this respect, Swiss Re sketched the insurance marketing channels and indicated "Tougher competition is forcing insurers towards greater innovation in marketing in Latin America. The most important new approaches are distributions via the banks (bancassurance) and use of the internet to back up sale efforts. Essentially, however the Latin American insurance market is still dominated by brokers, agents, and in life, also by insurance company's own field representatives", Sigma Nº 2/2002.

Any Colombian citizen or foreigner residing in the country may exercise the profession of agent and agency.

Insurance Brokers. These are companies organized as a limited liability company or stock companies whose corporate purpose is exclusively to offer insurance, to promote its execution and to obtain its renewal acting as intermediaries between the policyholder and the insurer (Art. 1347 of the Commercial Code and Art. 40 FLFS). In Colombia, the concept of insurance brokers as a natural person does not exist.

To operate, insurance brokers have to be registered with the Superintendence and have a "certificate" that proves them to be brokers (Art. 1349 of the Commercial Code).

To register, the company will have to demonstrate that its associates and managers are suitable persons and to declare, under oath, that neither the company nor the associates incur in inability or incompatibility.

To form their companies, insurance brokers are required to have a minimum capital of US$ 104,000 readjusted annually according to the CPI, an amount equal to US $107,000 at June 2007 (Colombian $205.000.000). In operation, the brokerage company will have to have a minimum capital equal to the largest total between 10 % of the intermediation incomes of the previous year and US$ 107,000 (number 1.2. External Circular 007, 1996). A Civil Responsibility policy (Professional indemnity policy) is not required as guarantee from the brokers because they must have a minimum capital. It is usual in other jurisdictions that such insurance policy be demanded from the insurance brokers to cover potential damages that they could cause to the policyholders.

The Commerce Code establishes that the commission of the insurances broker must be paid by the insurer (Art. 1341, Commerce Code). This means that it is not possible to have a broker where the client pays a fee for advice.

Agents. They are natural persons who promote the execution of insurance contracts (and capitalization contracts as a form of contractual savings) and the renewal of these. Agents could work with one or several insurance companies (or capitalization companies) (Art. 41, Number 1, FLFS).[25]

The agents can be dependent or independent agents (Art.41, number 5, FLFS). Dependent Agents are persons that have entered into employment contracts to execute the work of agent with an insurance company or a capitalization company, promoting and selling their products. Independent Agents are persons who, by their own means and by a commercial contract, dedicate themselves to the promotion and selling of insurance policies and of capitalization securities, without dependency on the insurance company or on the capitalization company. In this case the agent will be able to enter into contracts with several insurance companies or capitalization companies.

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[25] Capitalization companies offer saving securities with a short term defined, suitable for low saving capacity people. Legislation separates them from other contractual saving entities like insurance companies and pension funds.

At present, legislation does not demand that agents must be registered with the Superintendence and the majority of agents operating in the market are independent agents. Insurance companies are responsible for making sure the agents meet the competency requirements for exercising their profession (Article 101 Law 510, 1999, part 2). Competency refers to having sufficient knowledge or experience in insurance, and the insurance companies must certify that they have trained the agents to the point of reaching competency (Art 3 Decree 2605, 1993). The training programs held by the insurance companies must be made available to the Financial Superintendence.

Insurance Agencies. Agencies are administrative organizations specializing in the selling of insurance. According to the Law, insurance agencies are representatives of insurance companies; they can represent one or several insurance companies in a certain territory. The insurance agencies can be directed by natural persons and by legal persons (Art.41 numbers 2 and 3, FLFS).

- Conversion of the insurance agencies: The agencies must turn into insurance brokers if during the previous annual exercise they have produced commissions equal or greater than 800 *legal minimum monthly wages* (LMMW). For 2007 this amount is US$173.600. In that case the company would be supervised by the Superintendence.

- The agencies must have the following faculties granted by the insurance company or companies that they represent: to collect premiums, to inspect risks, to intervene in salvages and to promote insurance sales (Art. 42, FLFS).

- The insurance agencies must have a public certification (regulation elaborated by the agency) in which their minimum powers are stipulated), which must be put up in a visible place in the agency's offices.

The commissions, means of payment and other conditions are agreed between the agent that intermediates and the insurance companies (Art 207 Nº 2 FLFS).

Responsibility for the acts of the agencies and insurance agents. Insurance brokers are supervised by the Financial Superintendence. An insurance company or a group of insurance companies are responsible for the designation and for the acts of the agency and for the agent in the execution of their functions. Responsibility for the performance of the agents and the agencies falls to the own companies; since 2005 these are not supervised by the Superintendence. The companies are jointly and severally liable (Art. 54, Nº 4, FLFS and Law 510, 1999).

The regulation establishes the suspension of the activity of the brokers, agents and agencies for the following actions, among others: i) The violation of any legal or regulatory norm on insurances; ii) selling insurance under a plan other than the one offered, deceiving the policyholder (The policyholders could think that they are buying a different coverage) ; iii) offering benefits that the insurance policy does not guarantee; and iv) the transfer of commission in favor of the policyholder (Art. 207 Nº 2 FLFS).

4.1.2.2. Other marketing channels

The Superintendence regulates the relationship between credit entities (lending institutions such as banks and others) and insurance companies (*bancassurance*), including insurance intermediaries. However, originating from new distribution channels, which operate mainly through collective policies, has led the authorities to clarify the conditions for distributing insurance products by channels like public utilities. Besides, legislation on the cooperative sector also looks upon cooperatives as distribution channels.

Described in this section are other entities associated to micro-insurance in addition to insurance companies and intermediaries. Besides the insurance sector as the core sector, the bank sector, the solidarity economy sector (including cooperatives and employee funds)and MFI's, particularly NGO's specialized in microcredit, and public utilities companies are being used as microinsurance distribution channels.

Credit entities (e.g. Bancassurance). The insurance companies and the insurance intermediaries under their responsibility can, by means of a "remunerated contract", use the office network of credit entities (mainly banks) for the promotion and management of operations related with insurance selling. (Article 5 Law 389, 1997, Article 3 Decree 1367, 1998, and Law 510, 1999). Worth mentioning is the fact that other banking institutions are embracing the distribution of micro-insurance and that they are an important potential channel of distribution along with the non banking branches. This is the case of Megabanco that, with Aseguradora Solidaria, offers funeral insurance and life insurance with benefits in money to buy food and to pay school. Megabanco also offers an insurance to pay some credit installments in case of non voluntary unemployment. In addition, Bancolombia and Bank BBVA recently announced their plans to commercialize life microinsurance s and other products.

Regulation limits the types of products that may be sold via credit entities to those that are considered "suitable". Insurance products that have the characteristics of universality, simplicity and standardization are considered suitable for commercialization through this channel. This kind of product could be commercialized on a large scale as it does not demand specific conditions as regards the persons or insurable interests. The following kinds of insurances are considered suitable to be distributed by bancassurance: the Transit Accident Compulsory Insurance, Homeowners' Insurance, Multiple Line Insurance, Vehicles, Funeral Insurance, Personal Accident, Unemployment, Education, Individual Life, Voluntary Pensions and Health Insurance. (Decree 1367, 1998, Art. 2).

For that purpose the insurance company may have to adopt the necessary measures so that the public can identify it clearly as a legal person different from the bank or any other credit entity. This means that the client must know that the product is provided by the insurer and not by the bank.

The "administrative expenses" incurred by the insurer by using the bank network to distribute the insurance include the service of premium collection.

The insurance companies are authorized to use the *credit entity or bank personnel* for the insurance promotion and management work. (Art.5, Law 389, 1997).

Banks offering micro credit and financial services to low income people (different to bancassurance). Of the 18 banks that operate in the country, one is state-owned (Banco Agrario). This bank and Banco Caja Social Colmena have a great experience serving low income people. Particularly the latter that has been acting as a distribution channel through its micro credit advisors that specially establish direct contact with micro entrepreneurs. Considering that they are simple products, these insurances are offered by sales forces specializing in micro finance who offer credit and insurance.

Micro Finance Institutions (MFI). In Colombia there are a large number of MFI that specialize in micro credit and others that combine this activity with the providing of social support, educational and productive services. These institutions are NGOs that are not supervised by the Financial Superintendence or any other superintendence. These NGOs must comply with the rules for non profit organizations. In general terms, the development of this marketing channel lies in the fact that the policyholders receive some education about microfinances including microinsurance and they have a premium collecting mechanism (savings account, etc.).

Among the MFIs, the most relevant are the Banco de la Mujer network and a series of institutions grouped under the Emprender network. These institutions have developed micro credit programs in many parts of the country, although with a limited coverage, because a high portion of the population has no access to these services. Nevertheless, because of their social purpose, these organizations were able to serve segments of the population that had the lowest income and that traditionally are not served by formal financial intermediaries. Also, because of the closeness and the group of services they offer, they achieve a broad knowledge of the needs of these populations, which represents a great potential for developing more adequate and efficient instruments.

Simultaneously with the micro credit activity, some of these MFI have served as microinsurance distribution channels for their clients. The case of the World Women's Foundation in Bucaramanga, affiliated to Women's World Bank, and that of Oportunidad Latinoamérica Colombia, OLC, in Bogotá are examples of the use of these channels and their cases will be studied later. These entities provide microinsurance for their clients through insurance brokers and as well as insurance companies directly.

In fact, insurance cooperatives have used the cooperative network and MFI to distribute microinsurance. These distribution channels are responsible for the marketing, collection of premiums and other customer services; they participate in the revision of claims and make payment of these on behalf of the insurer, charging a fee (around 25%). On its part, the insurer absorbs the risk, fixes the prices, pays the compensation and makes sure legal requirements are fulfilled. The success of this model not only has been in the size of the cooperative system but also in general, the insurance cooperatives and MFI deduct the premium from the credit or a current account with the institution that intermediates the insurance.

Family Benefit Funds. These are nonprofit, private law persons, organized as corporations in the manner established in the Civil Code. They fulfill functions related to well-being of workers through the collection of contributions and payment of a Family Subsidy Allowance benefit and develop social welfare programs. They are funded with a percentage of the payroll (compulsory), paid by the employer as a quasifiscal contribution. Thus, these funds only serve people that are formally employed and on a payroll. There are 55 Family Benefit Funds and they are supervised by the Family Allowance Superintendence. Family Benefit Funds are being used as microinsurance distribution channels (see Table 12 on a personal accident insurance policy sold through a Family Benefit Fund).

The Cooperatives as market channels. The legislation for cooperatives established that insurance cooperatives do not have to uses agencies, agents or insurance brokers to sell insurance. This means that the insurance cooperatives can put their policies on the market using other channels of distribution that could be their own cooperative system and other entities of the solidarity economy system (Article 74 Law 79, 1988). Nevertheless, the cooperatives can work with intermediaries that are regulated by FLFS.

Information raised between companies in the market indicated that cooperatives and entities of the solidarity economy sector that distribute and administrate insurances charge the insurance company approximately 25% of the premium as payment of administrative expenses.

Public utilities. There is a secondary regulation that was issued to clarify some topics related with charges that public utilities companies (companies that provide expendables such as telephone, light, water and others) can include in their invoices. That regulation made it easy to use utilities as insurance distribution channels, working through collective policies.

- In 2005 the Council of State (the high court to deal with controversies arising with different State entities) indicated that it is possible to include on a residential public utility bill the payment of a good or service that is not inherent to the utility provided, as long as it is authorized by the user (File Nº 250002326000200401186801, March 3, 2005).

- Later, on September 6, 2006 the Financial Superintendence stated its position about offering insurance policies through residential public utility bills based on the Ruling by the Council of State (letter registered with No. 2006031381-001).

- Lastly, on March 15, 2007 the Ministry of Trade, Industry, and Tourism issued Decree 828, 2007, which once again outlines what was established by the Council of State in 2005.[26]

With regard to this matter, legislation established that insurance policy payment can be included in the bill of the public utilities company only if the users authorize it, i.e. client must consent to it. Also it was established that the charge value that is not part of the public utility service must be totalled separately, that the public utilities company cannot suspend or cut the service if the user does not pay the insurance premium.

The most successful example of distribution through "Public Utilities Companies", has been the case of Codensa with Mapfre. Codensa is an example of how to market mass products for all the strata. In this case, there has been an incentive for Codensa to sell the product:

[26] This decree contains rules in areas that contribute to maintain low inflation rates.

this public utility company is trying to build customer loyalty. Therefore, if micro-insurance is to be a success, channels need to be found that are interested in building customer loyalty or broadening their client base.

In this type of channel, providing support to the insured in procedures related to purchasing micro-insurance has been an important factor in its development. We have become aware that people with low incomes need to be guided and to be able to count on permanent support, which is why the role played by those who assist the families and the existence of a telephone line, 24 hours a day, seven days a week, during the 365 days of the year has contributed favorably toward the purchase of this insurance. According to information picked up in the market, similar experiences also exist, such as the Aseguradora Previsora with Aguas de Manizales and AIG with Gas Natural. The success of this model not only has been in the size of target market (utilities clients) but also in that the insurance regulation is suitable and utilities companies have been interested in creating service relations with their clients (client fidelity).

Other future marketing channels. Usage of other possible distribution channels such as hospitals, educational establishments (through parents' fellowships in public schools) and large retail businesses are implicity allowed but not regulated.

4.1.2.3. Regulation on electronic payments and e-commerce

Supervision of the financial intermediaries and the electronic payment networks is carried out by the Financial Superintendence. Decree 1400 of 2005 established the inspection, surveillance and control of the entities that administrate low value payment systems. Colombia has an electronic business law in accordance with the international standards found in the model law of the UNCITRAL (United Nations Commission on International Trade Law) designed by the Organization of the United Nations. Based on this law, Colombia issued law 527 in 1999 to support electronic transactions. The principal objective of the law is to incorporate a policy framework that guarantees technological development in the subject of e-business.

Development of electronic payment systems. Together with an improvement in the access to financial services, it is hoped that, in addition to the credit, there will be an increase in the use of means of payment other than cash. The new technologies offer electronic channels such as Internet, intelligent cards and mobile telephones that can make a very positive contribution toward improving access to the financial services and in particular to more efficient means of payment.

Colombia has the technology for using electronic means of payment; nevertheless, not all the possible options have been developed. The system of payment for low amounts is cash and check, fundamentally, although the use of electronic means of payment has increased in the past few years.

There are credit cards, debit cards and transactions can be made over Internet or the telephone. The use of cell phones as a means of payment has not been developed yet but projects are being evolved in this respect and some pilot experiences have been carried out in electronic money schemes. Nevertheless, the development of electronic money products has been slow in Colombia compared with the rhythm in other countries of Latin America. The operators of low value payment systems consider that the technology is available for introducing more sophisticated products such as electronic cash and intelligent cards. The limitations for this type of project lie in the implementation costs (change of data phones and cards).

The work of supervision and surveillance of financial intermediaries and electronic payment networks is carried out by the Financial Superintendence.

With regard to payments via Internet, all the leading banks use products based on EBPP (Electronic Bill Presentment and Payment). Several initiatives are in the pipeline for business to person payments (B2P Business to Person).

With regard to the development of payments through mobile phones, taking the service to a greater number of users at a reasonable cost so as to be able to use them as a means of payment is not necessary yet in Colombia. At present, not only the cost of a minute of telephony but also Internet access is too high for low income users. In fact, access to internet via this means is currently used by very few subscribers. In Colombia Internet penetration, measured as number of users/population, is barely above the average for Latin America (Figure 3). Also, the telephonic devices that have the technology to carry out these transactions are the most expensive and therefore less available to the low income population. It is important to note, however, that the number of activated cell phones has grown significantly in Colombia over the last four years. It is expected that by the end of 2007 there will be a total number of activated cell phones greater than 30 million. In addition, the majority of cell phone users are concentrated in income strata 1, 2, and 3 (72%):

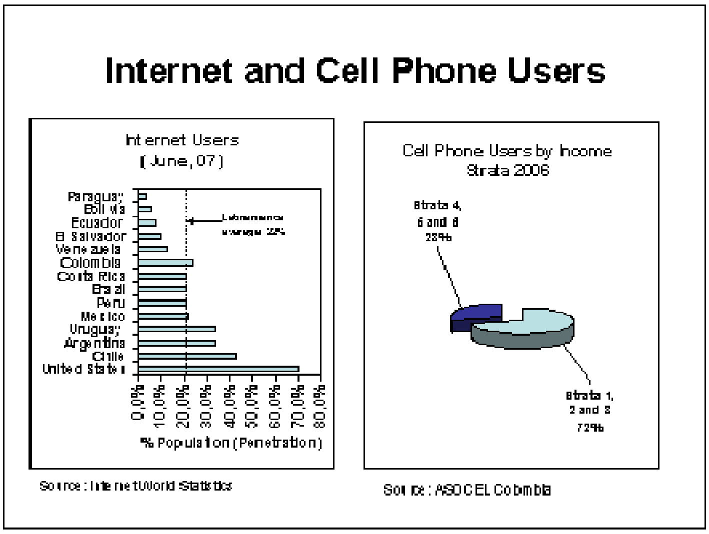

Figure 3. Internet and cell phone penetration in Colombia.

According to Arbeláez and Zuluaga (2006), in Colombia the operators of payment systems consider that there is no need to develop very sophisticated electronic payment products but rather those that already exist should be adapted to the realities of a market with a low purchasing power and reduced bank usage. In this respect, the challenge lies in increasing the coverage of the financial services, access to Internet and the use of these means of payment instead of incurring in expensive investments.

In the Colombian case, the development of cellular telephony as a means of payment under the scheme of prepayment cards that do not require users to make use of bank services, could contribute significantly toward improving access to financial services for those segments of the population that have lower incomes.

To bring the use of electronic payment means to the masses, it is important that people become used to using these schemes. To reach this objective, the users must become familiar with the tool and they must be convinced that these are safe channels of payment.

From the point of view of the development and mass market roll-out of micro-insurance, the above shows that although Colombia has various means of electronic payment these are not easily accessible to persons with lower incomes. The development of these means of payment does not necessarily have to be linked to an increase in bank usage. The objective must be access to payment technologies that are cheaper. The lack of instruments like prepayment cards would be delaying a more efficient distribution of micro-insurance among the poor because there would be no possibility of collecting the premiums more easily, especially in the regions that are more distant from the urban centers.

4.1.3. Regulation on market conduct, consumer protection and corporate governance

Regulation on market conduct. In this topic the following matters were reviewed: i) the regulation related to authorization for selling products (market insurance policies); and ii) regulation on consumer protection.

Requirements for submitting insurance policies and "authorization of maximum charges". These requirements are regulated in External Circular 007, 1996 and Art. 184, Nº 1 FLFS, which establishes that the prior approval of "insurance policies and charges" by the Superintendence is only necessary in the case of granting the initial authorization to an insurance company or when the development of a new product is authorized.

The general rule establishes a freedom of policies and tariffs. The insurer must submit the models of insurance policies to the Superintendence before using them. The model text of the policies must be registered beforehand in the "Model insurance policies and annexes deposit" of the Superintendence, which must be at the disposal of the public in general.

Premiums for underwritten insurance policies are freely set by the insurers, but must be submitted to the Superintendence before use, for ex post supervisory purposes. The insurance companies must maintain the tariffs at the disposal of the Superintendence classified by branches, together with the relevant documentary elements and statistical supports. From the year 2000 only life insurance can be sold in dollars (Art.79 Resolution 8, 2000 of the Central Bank).

The rates must comply with three rules: i) Observe the technical principles of equity and sufficiency; ii) Be the result of the utilization of statistical information that complies with the requirements of homogeneity and representativeness; and iii) Have the backing of reinsurers with a proven technical and financial solvency.

Regulation on consumer protection. The regulation on consumer protection considers different matters related with contracting insurance linked to loans and the client defender scheme (Section I, External Circular 007, 1998 and Decree 690 of 2003, on “Client Defender”).

Freedom to contract insurance linked to loans granted by financial institutions. The regulation comprises mechanisms to protect insured. Financial institutions (banks and others) are authorized to contract insurance on behalf of their debtors. Financial entities must adopt acquisition procedures and report them to the Superintendence, in order to guarantee the free participation of all insurance companies in the process. These procedures must detail the diffusion means through which the insurance companies are invited to present proposals. The Superintendence verifies the fulfilment of the procedures and the financial entities will have to inform the Superintendence whenever they are going to begin to contract insurances.

The regulation also considers protecting the policyholder’s freedom to contract fire/earthquake insurance policies linked to credits and also to choose the intermediaries. The insurance policy presented by the debtor cannot be rejected based on the existence of an insurance taken out by the institution. This means that the credit provider may insist that the debtor takes out insurance, but may not insist that the debtor takes their insurance. Besides, banks must make known the policy conditions and premium to each debtor (Part 2, Art 120, FLFS).

Client Defender, claims and complaints. In accordance with the FLFS and Decree 690, 2003 insurance companies, insurances brokers and insurance agencies must appoint a client defender that carries out activities related with client protection, which is paid by the insurance companies. The client defender may perform these functions for several entities simultaneously. Since the activities of the agency and of the insurance agents that affect their clients are the responsibility of the insurance companies, matters related with claims and complaints fall within the jurisdiction of their client defender.

The insurance companies must send the Financial Superintendence complete information on the identity of the client defender and a half-yearly statistical report on the number and type of complaints.

A function of the client defender is to act as spokesman of the clients before the insurance company and to know and to resolve, freely and objectively, the individual complaints that these present to him. The Superintendence is responsible for overseeing the client defender’s obligations. The performance of the client defender is independent from that exercised by the Superintendence. The decisions of the client defender are not compulsory for the company or for the client; nevertheless the insurance companies will be able to establish in the norms on corporate governance or internal regulations that they are obliged to fulfill decisions that are favorable to the client and accepted by these.

The Financial Reform bill that was submitted to Congress seeks to give the consumer more guarantees. With the reform, the client defender will be appointed by the FS instead of the financial entities and they must create a System of Client Service, among others topics.

Regulation on marketing. Regulation also controls the manner in which insurers may market their products. If insurance companies share publicity with other unsupervised entities, the regulation requires that the insurers' name be displayed clearly. Features like the location of the logo and size of the insurance company name are defined in the regulation. Insurers are forbidden to offer conditions or insurance benefits that are not expressly contained in the insurance policies (External Circular 7, 1996).

Regulation on advertising. The general rule of advertising established that when an institutional campaign is carried out, the insurer needs no ex ante authorization from the Supervisor. But, when the campaign is related to its particular products, it needs to be sent to the supervisor for ex ante supervisory purposes.

Regulation on corporate governance and other matters. With regard to corporate governance, specific regulations have not been issued in the Colombian insurance market forcing insurance companies to adopt corporate governance rules. However, Fasecolda, the association of insurance companies, issued a Code of Good Practices in July, 2007.

The authorized risk agencies carry out the Qualification of Claims Payment Capacity for the insurance companies. (Res-1063, 1998, Art. 2.3.4.1., letter d). For the insurers, risk classification is voluntary. The insurer can accept, appeal or reject the qualification. Equally it can sustain private qualification until it decides to make it public. If the company wants to make the qualification public, the agency executes an analysis report that is published and that is sent to the Superintendence, to the mass media, to the institutional investors and to any person who requests it.

Finally, insurance companies can outsource the administrative, accounting, personnel administration, treasury and investment handling functions. This because there is no regulation that prohibits it.

4.1.4. Tax regulation and regulation on money laundering

Tax regulation. There is no special tax treatment for microinsurance products in Colombia. Hitherto the government has fulfilled the Banca de las Oportunidades policy without any tax incentives, mainly as a result of the fiscal adjustment long term goal. Thus, it is unlikely that the Colombian government could use tax incentives to promote microinsurance development.

The regulation does not establish a different income tax treatment for insurance corporations and for insurance cooperatives so the income tax rate is the same; 38.5% for both kinds of insurance entities.

A person that buys an individual policy may deduct the premium paid for insurance from the taxable basis for Net Income of the Income Tax. This deduction applies to life and health insurance. Besides, the indemnity that the beneficiary of a life and damages insurance receives, with the exception of compensation for lost profits, does not constitute income.

Insurance premiums are subject to different VAT rates. Property insurance is taxed with 16% and hospitalization and surgery insurance, and health insurance in general, are encumbered with 10%. Life insurance, personal accident insurance and, in general, life and personal insurance that is not health insurance, are exempt from VAT. Insurance related to the social security system, is also exempt from paying VAT. The reinsurance paid in Colombia is exempt from paying VAT.

Finally, in Colombia the users of the financial system and the entities that form it are subject to a tax on the total value of the financial transactions executed, named Financial Transactions Tax (Gravamen a los Movimientos Financieros in Spanish). This is a bank debit tax applicable to all withdrawals from current and savings accounts and other financial assets. The tax rate is 0.4 % (4 x 1000).

Cash transactions and some specific transactions are tax exempt. The exemptions seek to correct regressive effects of the tax. The tax burden could be high if lower income people execute more transactions during a given time. Thus, withdrawals from savings accounts that do not exceed US$3,500 (Colombian $7,000,000) monthly are tax exempt.

The exemption only applies to one exclusive savings account owned by a person or small business. This account is marked and managed by the financial institution, which must submit the information on transactions to the tax authority. Additionally, the withdrawals made by pensioners from the financial entities that administrate their respective monthly pensions are exempt.

Regulation on money laundering. The norms on money laundering establish demanding procedures with the objective of establishing client identity, among other things (External Circular 7, 1996, Chapter XI, First Title). The insurance companies must know the client and this obligation commences from the moment that a person is linked to the insurance company as a client. In this respect, the following must be complied with:

- The insurance company must have the client fill out a “client interrelationship form” and verify and make sure that the mentioned form is processed adequately, i.e. it is necessary to provide careful responses to the extensive information requested about identification of the client and his economic situation.

- Insurance companies are not obliged to demand the form for insurance related to social security, the SOAT, personal accident insurance, insurance whose beneficiaries are government entities, insurance of legal cases, health and funeral insurance. Thus, non life and property microinsurance products are under the money laundering requirements.

- Filling out the form is not obligatory for insurance taken out via mass marketing or bankassurance provided that payment of the premiums takes place by means of a direct discount in a savings account, checking account or credit card, and that the client has given specific authorization for the transfer.

- Knowledge of the client also supposes that an interview has taken place with the future client. A record must be kept of the date, time and result of the interview.

- As of January 2008, a system must be implemented for administrating Asset Laundering Risks and the Financing of Terrorism.

Therefore norms on money laundering could be restrictive to microinsurance development. From an analysis of the regulation and of opinions picked up in the market, one concludes that although these rules protect the utilization of insurance in money laundering, in the case of microinsurance these rules do not make its development easier, because microinsurance requires simple sales procedures. The requirement of an in-depth knowledge of the client through filling in a form and holding a personal interview, means asking the possible insured for too much information which will lead to greater costs and the difficulty of obtaining information that poor people do not handle or know. As was mentioned, the regulation exempts funeral, accident and health insurance from this obligation; but not life insurance, and insurance of assets must comply with this rule.

The persons who pay for premiums authorizing that the discount be made from their savings account, checking account or credit card are not obliged to fill in the form either. However, this exemption is not necessarily a solution to facilitate microinsurance development because Colombia has a low bancarization level. In fact, one of the most successful distribution channels for microinsurance to date has been carried out through the public utilities companies, in which case there is no credit in favor of the insured that would permit discounting the premium.

In the case of microinsurance these rules do not make its development easier, because microinsurance requires simple sales procedures. The possibility of setting a maximum premium amount below which the asset laundering regulations would not apply, could be studied. In fact, financial services to people covered by Familias en Acción program, which is a program of social assistance for families in extreme poverty managed by the President's office, are exempt from the rule of knowing the Client (External Circular 061, 2007).

At the moment, to conclude this study, Fasecolda was discussing the setting of a maximum yearly premium below which the money laundering and financing of terrorism rule would not apply. The proposal is that this maximum could be estimated in terms of the minimum monthly wage.

4.1.5. Overview of government's policy on insurance and inclusion in general

In 2006 the Colombian government has implemented a policy to enhance access to financial services, especially for poorer people. This fundamental investment program is called Opportunity Bank, *Banca de las Oportunidades* in Spanish. At interviews with government authorities related with financial services (the Minister of Finance and the Financial Superintendent, among others, see Appendix 7) conducted as part of this review they expressed their total support to the promoting of the development of Micro-insurance products. However, authorities noted that the development of Microinsurance lies in the private sector and that a government policy to subsidize the activity will not be adopted in spite of government support to microinsurance. Also, the high authorities of Ministry of Finance as well as of the Financial Superintendence noted that they are willing to review any matters necessary to facilitate a speedier development of microinsurance.

Banca de las Oportunidades: a government policy. The government of president Uribe has identified micro finances as a fundamental factor in its poverty reduction policy and to enhance equity. With the fostering of microfinance the government is also promoting a higher level of bancarization especially among poor people. The government is seeking a higher use of the formal financial sector in low income people not only through credit and savings, but also as a channel to strengthen payments systems and a way to access insurance products (Figure 4).

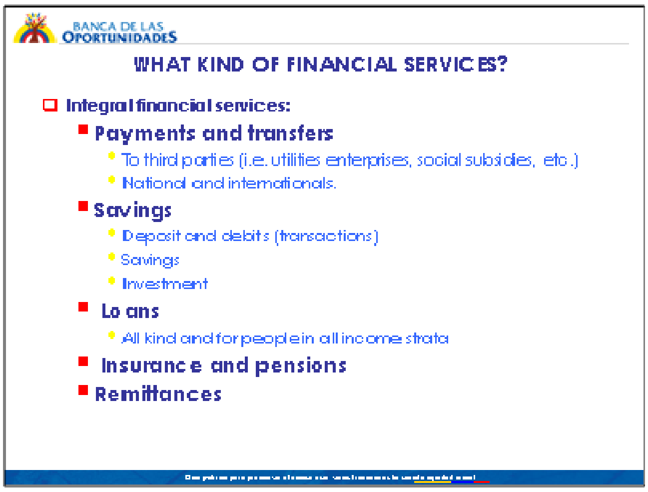

Figure 4. Overview of Banca de las Oportunidades

The Banca de las Oportunidades policy has an investment program created in September, 2006 (Decree 3078, 2006) and managed by Bancoldex.[27] The program aims to enhance access to financial services, particularly for low income households, in order to promote development with social equity. The program includes overall financial services which are payments and transfers, savings, loans, *insurance* and pensions and remittances. The program is carried out by a network composed of banks, commercial finance companies, NGOs specialized in micro credit, financial cooperatives and Family Benefit Funds.

The government will intervene through three levels. In the macro level the government will work in regulatory aspects to enhance access to financial services. In the intermediate level the government will carry out support activities aimed to strengthen infrastructure for microfinance institutions (technology providers, information institutions on risk, warranties, and financial education programs, among others). In the micro level, the government will support activities of banks, commercial finance companies, cooperatives and NGOs to give them incentives to expand and design broad-based financial services.

[27] Bancoldex is a government second tier bank that mainly provides financial services to exporters.

The correspondent banks. One of the benefits to microinsurance under the framework of the Banca de las Oportunidades policy is that, the government established the provision of services by credit establishments through *correspondent banks* (Decree 2233, 2006). These correspondent banks are to be connected through a data transmission system and will act on behalf of the credit establishment. The services that can be offered through the correspondent banks include receipt and transfer of funds, sending or receiving drafts in Colombian currency within the national territory, and deposits and withdrawals in cash from checking accounts, savings accounts, or term deposit accounts. They are also allowed to make the transfers that affect said accounts, answer balance inquiries for checking and savings accounts, and make disbursements and cash payments for active loan operations. Note that the permitted actions for correspondent banks *do not include the sale of insurance; they only could collect insurance premiums*. This is a service that could be included in the legislation in order to strengthen microinsurance distribution channels, especially in very poor urban areas and remote regions.

Bancoldex officers in charge of Banca de las Oportunidades program view insurance as fundamental tools in getting people to leave poverty behind. This, from the perspective that even when they have been favored with micro-credit programs, if they are faced with an unexpected event that affects their lives, they will fall back into hardcore poverty just the same. Those persons whose lives are based on the development of businesses using micro-credits may lose everything they have gained if the head of the household should die, suffer a disability or the deterioration of his/her work tools. The importance the government is currently attributing to the development of micro-insurance is based on this approach. One of the ideas that is being shuffled is trying to direct the savings that arrive via remittances, which very often are not spent on real benefits for the poor. There have been suggestions in relation to channeling part of those savings to housing and insurance; therefore counting on products designed especially for the needs of poorer persons would be fundamental.

4.2. Supervisors and any other statutory bodies impacting on insurance

In Colombia, in addition to the Financial Superintendence that is the agency in charge of the insurance market itself, we must mention the Solidarity Economy Superintendence because of its link with entities that are related to the insurance sector, that is, financial cooperatives as well as non financial cooperatives under their control that participate in the distribution of insurance (see Box 3).

Financial Superintendence of Colombia (FS). The FS was created in 2006 through the merger of the agencies in charge of supervising financial institutions and institutions in the stock market. The former, called Banking Superintendence was created in 1923. The FS is a technical agency assigned to the Treasury Ministry, with legal status, administrative and financial autonomy and its own patrimony. The Superintendence's target is supervising the Colombian financial system in order to preserve its stability, safety and confidence, as well as to encourage stock market development and the protection of the investors, savers and policyholders. The Colombian authority has followed the regulatory model that brings together in only one institution the supervision of the three most important financial sectors: bank sector, security sector and insurance sector. Additionally, in Colombia unlike other Latin American countries, the FS also supervises the pension funds (Art. 325 FLFS).

Considering the importance that pensions systems have had in Latin American countries, in many of them the pension funds are supervised by a specific Superintendence.

Solidarity Economy Superintendence (SES). The SES was created by Law 454, 1998 as a technical agency of the State assigned to the Treasury Ministry (Art 33 Decree 454, 1998), in charge of the overall supervision of solidarity economy entities like financial cooperatives, non financial cooperatives, employees' funds and mutual entities, among others. Principal Superintendence target is protecting the interests of the cooperative's associates, of third parties and of the community in general. Financial cooperatives providing services to associates and non associates are supervised by the FS.

5. Market analysis

5.1. Microinsurance in Colombia

5.1.1. Providers and penetration

In Colombia, microinsurance has grown significantly since 2005 impelled on one hand because insurance companies have seen a profitable market opportunity among low income social strata and on the other by the government policy to encourage micro credits and financial inclusion.

As was mentioned in Section 3.1.1, since the end of the nineties the Colombian banking sector has undergone a movement down-market (commercial banks moving into microfinance) as many banks in other Latin American countries after the liberalization reforms. In Colombia this trend was reinforced by the financial crisis at the end of the nineties. Many commercial banks entered the field of microfinance looking for new markets. Among the main reasons for adopting this strategy, worthy of mention are increased competition, reduction of margins in traditional segments of the market, the positive experience of NGOs, MFI and financial cooperatives, as well as a wide segment of the market to be served. The banking strategy on the one hand, allowed insurance companies to offer mandatory insurance linked with micro credit, and on the other hand was reproduced by many insurance companies to provide other insurance products.

The financial sector strategy has been strengthened by the government policy to encourage micro credits that was consolidated in 2006 through "Opportunities Banking Program" (Programa de la Banca de las Oportunidades). Thus, the demand of an insurance linked with a micro credit has allowed promoting the microinsurance and other life and property insurance have been designed for low and medium income people.

In Colombia there are 30.5 million people living with less than US$2 per day, one of the World Bank's poverty indicators. According to Fasecolda estimations 8.4% of the BPP would be covered by some microinsurance product. This proportion is equivalent to about 2.6 million people.[28]

[28] Martínez, J., González, A. and Restrepo, J.M. (2007).

Based on the preliminary data of Fasecolda for the year 2006, the policies (2.7 millions) are distributed as follows: 60% property insurance, 24% funeral, 14% life and 2% professional liability insurance. Given the distribution of these insurances and based on interviews with market players, there are reasonable doubts about the high participation of property insurance because this classification would include cell phone insurance. Most of the cell phone insurance does not belong to insurance sold to low income people. Some market analysts suggest that there is no development of property microinsurance (assets). However, there is no better data available.

Microinsurance participation would reach 5% of the insurance market, including cell phone insurance. Considering that the total number of premiums of the insurance industry during 2006 amounted to US$ 3,204 million, the premiums for microinsurance were US$ 160.2 million.

An important share of domestic as well as foreign insurance companies in the market (41%) is offering some kind of microinsurance product. These products have monthly as well as annual coverage, though premiums payment is made mainly on a monthly basis. In fact, a survey performed by Fasecolda showed that 56% and 39% of the persons in strata 2 and 3, respectively, prefer to pay premiums on a monthly basis.

With regard to the channels of distribution used to sell microinsurance, in 2006 22% of the policies were sold through cooperatives, 18% through NGO's specialized in micro credit, 18% are direct sales, 11% bancassurance, and 9% through the public utilities bill.

5.1.2. Characteristics of microinsurance products

As was mentioned above, at the beginning the products offered were linked to the typical insurance captured by micro credits (credit life insurance); nevertheless, now there is a supply of microinsurance products focused on low income people, including micro and small business.

The design of this type of product has considered the unique needs of Colombia's poor people. Table 12 presents a brief overview of some models of microinsurance products offered on the Colombian market through different distribution channels. The lowest monthly premium is US$0.42 for funeral services reaching US$4 for life and asset insurances. According to Fasecolda research, a high share of premiums offered at the moment are concentrated in a range between US$2 and US$3.

As is expected the insurance cooperatives (Solidaria and Equidad) have been pioneering in microinsurance s, as they are the insurers nearest to the organized low income sectors (cooperatives and NGO's). At the beginning, Solidaria and Equidad offered the financial cooperatives and the NGO's the credit compulsory insurances that protected them against the possible death of debtors. Subsequently they started to offer voluntary life insurance to the clients of these entities.

Insurance cooperatives as well as insurance companies have designed products that cover both the assets and the life (included disability and health) as an integral family protection. Some examples of microinsurance offered by two companies of the market are shown in

Table 12 below. Its aim is to make known some products that they are currently marketing, as well as inform their premium level. As it is about different coverages, making a rate comparison is not the purpose.

Some examples of micro insurance products offered in the market and the distribution channel
June, 2007

Type of product	Coverage plan	Monthly premium (US$)	Automatic coverage (US$)	Target Market
Life credit policy (compulsory)	Death for any cause, total and partial disability, and serious illness	1.5	5,200	Clients of NGO's specialized in micro credit
Life policy	Funeral service	0.42 to 0.70		Clients of a financial cooperative
	Death for any cause, total and partial disability, additional indemnity and	1.7 or a yearly premium that excludes funeral services by 19.8	2,599 (for any of these events)	
	Daily rent for hospitalization		7,800	
	Intensive Care Unit		15,600	
	Medical treatment and ambulatory surgery		3,900	
	Childbirth		7,800	
Asset protection	Fire Robbery Theft of money inside the property Electronic Equipment Civil Liability	1.0	2,600 520 260 260 2,080	Clients of a NGO's specialized in micro credit
Family protection	Death Total and partial disability Daily rent for hospitalization Serious illness	4.0	5,200 5,200 10 2,600	Clients of a NGO's specialized in micro credit
Personnel Accident Insurance	Accidental death */ Total and partial disability*/	3.1	15,595 */ 15,595 */ Funeral service for US$520	Affiliates to a Family Benefit Fund
	*/ Includes an education fee of US$260 on a monthly basis for each son during 12 months */ Includes coupons to purchase groceries for US$520			
Asset protection of Small and Medium Enterprises	All risk material damage Robbery Machinery breakdown Money and securities Civil Liability	Between 4.06 and 4.34 with funeral service or	2,600 1,040 260 260 2,080	Clients of a NGO's specialized in micro credit
Life	Death Total and partial disability	Between 2.95 and 3.23 with funeral help	520 520	
Funeral assistance	Policy holder, husband/wife and children		182 by each person	
Life insurance	Death for any cause Total and partial disability, and serious illness Help for home expenses for death	3.3	3,275 3,275 275	Clients of a Public Utility Company (Codensa)

Source: La Solidaria insurance cooperative and Mapfre insurance company

Table 12. Overview of microinsurance product examples

<u>Examples of some of the innovative products included:</u>

- *Insurance tailored to small business.* Mapfre has offered to Emprender, a network formed by 33 cooperatives and NGO's that provides micro credit mainly to micro enterprises, an insurance focused on micro enterprises that guarantee the affiliate full coverage, because there are three insurances in one. These insurances protect the business (or enterprise) of the affiliate and additionally, in case the client dies or remains incapacitated, it guarantees his family cash compensation. It also grants the funeral service (or a cash indemnity) for the affiliate and his family group.

- *Distribution through public utility.* There are also asset protection products offered through mass distribution channels as a public utilities company (Codensa, an electricity company). Mapfre offers an insurance that guarantees, in case of death or disability, an indemnity to small businesses that paves the way for the continuity of the business and is an economic help to the family. In case of death or disability, 50 % of the insured amount is paid in cash and the outstanding balance in 12 monthly bonds.

- *Benefit payments targeting groceries and education fees.* Also the policy's design of these products considers the most suitable way for the policyholder to receive the benefit. There are accident insurances that in case the affiliate or his spouse dies or remains an invalid because of an accident the insurance guarantees his family a cash indemnity; plus a coupon to purchase groceries; plus a monthly fee for one year's studying expenses of every child under the age of 18, and plus the funeral services. The client can decide if food and education benefits will be paid on a monthly basis or in a single payment.

- *Accelerator benefits.* There is a life insurance product that in case the affiliate or his spouse dies for any cause including an accident or has a total or permanent disability, guarantees to the family a cash benefit, and also if they get a serious illness the insurance guarantees an advance of 50 % of the total insurance to begin treating his illness.

- *Products targeting migrant workers.* Liberty is a company that also has worked on designing products bearing in mind the particular needs of low income persons. For instance, considering the high emigration of Colombian citizens to United States and Spain they offer a product that gives coverage for repatriating the corpse of the relative who dies in those countries.

- *Cover for motorbikes.* In the same line, Liberty and other companies have had to work on products to cover motorbikes which are an important means of transport especially for low income people. In Colombia there are cities in which the proportion of motorbikes that circulate is larger than that of cars. The proprietors of these vehicles use the motorbikes for their transport, and also to work.

5.1.3. Microinsurance marketing and distribution system

Distribution is key microinsurance challenge. In accordance with the opinion of government authorities and insurance companies, in Colombia the main topic with regard to the development of a microinsurance market is the distribution channel through mechanisms that could group informal people, due to the economy having a high portion of informality. Besides, the distribution channel needs to be efficient in order to collect premiums with low cost. Boxes 3 to 6 to follow below present cases that illustrate microinsurance distribution channels.

Distribution extends beyond intermediaries recognized in regulation. As was discussed in Section 4.1.2, in accordance with the FLFS only brokers, agents and agencies are defined as intermediaries. However, the activity of insurance intermediaries does not prohibit insurances entities from accepting risks directly without the intervention of the intermediaries. In this respect, the Superintendence also regulates the relationship between credit entities (lending institutions as banks and others) and insurance companies (*bancassurance*), including insurance intermediaries. In addition, new distribution channels have arisen during past few years.

In Section 5.1.1 other entities associated to micro-insurance supply were described in addition to insurance companies and intermediaries. Besides the insurance sector as the core sector, the bank sector, the solidarity economy sector and MFI's, particularly NGO's specialized in microcredit are microinsurance distribution channels. In the solidarity economy sector besides cooperatives, Employee Funds are also distribrution channels. Family Benefit Funds and public utilities companies are also important channels. At the moment, insurance companies are investigating the option of distributing microinsurances through large retail businesses (such as department stores for middle and low income population) and small supermarket chains.

It is important to note that some of these alternative channels also link with regulated insurance intermediaries. Particularly Employee Funds and NGOs interviewed pointed out that they use intermediaries.

<u>Unregulated funeral parlours.</u> Funeral Entities also have an active participation in the market. According to information published by a Colombian magazine, there are at least 33 companies offering funeral services as well as funeral insurance. These companies are not supervised by the Financial Superintendence. In the year 2004, their estimated sales amounted to approximately US$80 million (COP$160,000 million). [29] These entities provide coverage to approximately 3,000,000 people, according to a Fasecolda opinion..

In the insurance industry there have been objections to this activity because they consider them unauthorized entities that do insurance business. Nevertheless, in the year 2006 the Financial Superintendence gave its opinion on this matter in "Concept N° 2006004784", based on Article 111 of Law 795 of 2003. In this document it pointed out that funeral services do not constitute an insurance business because this is a legal relationship that "does not constitute an insurance contract".

<u>Cooperatives and NGOs provide penetration into low-income market.</u> Despite the low bank usage level, traditionally in Colombia there has been a supply of financial services to microenterprises and low income people. These services are provided by some banks, commercial financial companies, cooperatives and NGOs. Cooperatives and NGOs focus mainly on low income people of the formal and informal sector.

The Solidaria insurance cooperative has used a financial cooperative as the distribution channel for its product Confivida. This single policy insurance provides coverage for several risks. The insurance cooperative has put its product on the market through "Confiar Cooperativa Financiera" under a broad-based marketing scheme, which allowed it to place a great number of policies with the members of Confiar directly during the year 2006.

[29] Journal "La nota económica", April 2006, Colombia.

Additionally, Confecoop, in its report for 2006, states that there are 27 cooperatives that provide funeral services. In this same report, it says that the most important cooperative funeral services network of the country is the “Los Olivos” network (owner of the La Solidaria insurance cooperative), which has 16 entities, both cooperative in nature as well as in ownership. At the end of 2006, the number of families protected by this network of services amounts to 670,000.

Distribution through banks and NGOs specialized in micro credit. The development of financial services for low income people has been focused on credit. Savings products are small and only concentrated in few institutions like bank Banca Caja Social Colmena, Caja Agraria and financial cooperatives supervised by the Financial Superintendence.

Since the year 2000 banks have entered a downscaling process to provide financial services, particularly credit, to micro and small enterprises and low income people, expanding supply to the low income market segment. NGOs provide a combination of credit and entrepreneurial development strategies because they are not permitted to collect savings. The NGOs named *bancos de la mujer*, affiliated to WWB, represent near of 80% of NGOs microcredit clients.

Box 3 and Box 4 illustrate the cases of NGO’s specialized in microcredit, and Box 5 presents the Banco Caja Social case.

Box 3. Case Oportunidad Latinoamérica Colombia (OLC)

Oportunidad Latinoamérica Colombia is a nonprofit non-government organization (NGO) that operates under the auspices of Opportunity International. OLC develops financial and training programs to support people, their families and the communities in which they live. The micro-credit methodologies used are: Trust Groups (groups of 15 to 35 people) and Individual Credits. Nearly all their clients belong to the income stratum 1 and include people who have been displaced by the violence. OLC estimates that 73% of its clients have never had credit or any relationship with the financial sector.

1. Micro-credits.

Trust Groups

The Trust Group provides loans with group guaranty. Each member of the Trust Group undertakes to comply with his installment and to be collectively responsible for the other members of the Trust Group in case they do not comply with their installments, signing a joint surety as guaranty for the entity. Different loan amounts are handled and an interest that is reasonable compared with the market.

The amount of the credits ranges between US$300 ($600,000) and US$750 ($1,500,000) for a period of 16 weeks. Payments are every fifteen days and during the repayment period the clients are offered training in areas related to their business. An obligatory saving of 10% of the value of the credit is required and, as was mentioned, the Joint Surety. The credits are directed to micro entrepreneurs of the income strata 0, 1 and 2.

Individual Credit

This is a credit granted to a micro entrepreneur in order to strengthen his microenterprise and it is granted only to clients that are OLC graduates, that is, they have passed through Trust groups. The amount of the credit fluctuates between US$750 ($1,500,000) and US$5,000 ($10,000,000) for a period between 8 and 18 months. Attendance at monthly meetings to pay the installment and receive training is required. The credits are directed at micro entrepreneurs of the 1, 2 and 3 strata.

2. Microinsurance

In addition to the credit, OLC clients are obliged to acquire a microinsurance to cover “life”, “funeral” and “credit”. OLC receives part of the premium paid by the clients to cover costs related to the collection and paperwork, among others. An insurance broker, “Centro Seguros” acts as middleman for these insurances, transferring the funds to the insurance company, and charging the latter a commission.

The granting of credits and insurance together was started in the year 2002. Nevertheless, at that time 4,500 life insurance policies were sold with the company Seguros Bolivar. In the year 2006, the insurance was granted by the insurance company Mapfre, selling 12,000 policies. In the year 2007, the insurance is granted by the insurance company Liberty, expecting a sale of approximately 17,000 policies. The average premium is of US$1 per month for a client that has an average credit of US$500. The premium is paid in advance and the granting of the credit is subject to total payment of said premium.

In the five years that the insurance has been in operation, there have been 9 losses and approximately 50,000 clients have been served and insured.

(Exchange Rate Approximate: US $ 1 = Colombia $ 2,000).

Box 4. Case: Fundación Mundial de la Mujer- Bucaramanga

During the eighties the network Women World Banking (WWB) gave technical support to the creation of a network of five NGOs named bancos de la mujer (Women’s bank). These institutions were created to support low income women with micro and small enterprises. In 1982 Banco de la Mujer de Cali was created, and after that Medellín and Popayán in 1985, Bucaramanga in 1986, and Bogotá in 1989.

Fundación Mundial de la Mujer in Bucaramanga, an NGO affiliated to WWB, carried out a pilot experience with an insurance product named Amparar, designed according to the needs of this institution. The institution signs a collective policy which is offered to its clients as a voluntary life insurance that could be financed with the credit value. The policy covers death and is independent of the debtor’s policy that covers the credit value and is compulsory. With a low annual premium (a premium between US$ 0.07 and US$ 0.42 of monthly minimum wage, covers between US$ 1,560 ($3.1million) and US$ 10,400 ($20.8 million). Clients could supplement the life insurance policy with support to funeral expenses, educational expenses and a monthly support for food during a 12 month period. This program started with an agreement signed in 2003 with La Equidad. (Insurance cooperative)

Since August 2006 the insurance was contracted with another insurance company Suramericana de Seguros (Insurance Corporation). The new insurer also offers the compulsory life insurance credit, and a voluntary life insurance. The latter insurance is extendible to the family group and it covers death, disability, serious illnesses, funeral expenses, and revenue for death or disability payable monthly for 12 months. The new company covers the same insured amount as La Equidad.

WWB, as holder of the collective insurance policy, is in charge of collecting and informing the premium. It must also inform Suramericana of the income and retirement of the affiliates.

The insured can execute the claims with WWB or directly with the insurance company.

In eleven months (August 2006 to June 2007) the insurance company insured 35,500 affiliates.

(Exchange Rate Approximate: US $ 1 = Colombia $ 2,000).

Box 5. Case: Banco Caja Social (BCSC)

The Banco Caja Social has been a leader in supporting the progress of individuals and micro and small business for several decades. This bank has also been a pioneer in the placing of credits in small amounts. At present, BCSC through the network of Banco Caja Social BCSC serves more than one million clients through its 122 offices in 42 cities of the country.

In the beginning, the bank acted as middleman for compulsory microinsurance s (credit life and fire and earthquake) linked to the microcredits granted by the bank. BCSC has since extended its offer to voluntary insurance, underwritten by Liberty. These insurances are for shopkeepers, mass life insurance with increased protection and integral insurance for the home, insurance that protects the assets of the business and vehicles, in those cases where they finance their purchase.

The bank only sells insurance to people who have a savings account or a credit, because the mechanism for payment of the premium is discounting said premium from the balance in these accounts.

Considering that they are simple products, these insurances are offered by sales forces specializing in micro finance who offer credit and insurance.

The premiums of the credit life insurance (compulsory) and the voluntary life insurance are approximately US$1.2 monthly and the bank is currently placing about 1,000 policies per month.

<u>Distribution through Public Utilities Companies</u>. There are several experiences of public utility companies marketing microinsurance for their clients. The most successful example of distribution through “Public Utilities Companies”, has been the case of Codensa in Bogotá. Codensa is an example of how to market mass products for all the strata. In this case, there has been an incentive for Codensa to sell the product because the company is trying to build customer loyalty. The company along with the insurance company has implemented a consumer service program specializing in microinsurance clients through a call center (Box 6).

Box 6. Case: Codensa

This is an alliance between an insurance company and Codensa, a utilities company that has stood out as a distribution channel for microinsurance. Its strong point lies in a broad portfolio of clients (200,000) of which about 85% belong to strata 2 and 3. Codensa started in the distribution of microinsurance in the year 2003; nevertheless in the past few years it has achieved its best performance by the mass distribution of Mapfre insurance company’s Funeral insurance. In 3 years it has managed to increase placement of the funeral service insurance to 180,000 clients in Bogotá, which represents 90% of Codensa’s portfolio of clients. Premium of funeral insurance is of US$ 2.4 ($4,850) and the family group is insured.

At June 2007, the funeral insurances have granted about 4,300 services, a cost which on the average, for a family that is not insured, could be about US$ 2,000 ($4,000,000) per service. There are numerous testimonies of the benefits of the funeral assistance insurance offered by the company and support, as well as its humane and social responsibility side.

The strategy chosen for the sale of this insurance is to offer it through a flier attached to the receipt charging for the electricity service and the acceptance of the client-insured is required in order to make the sale effective. This acceptance is obtained in two ways.

- The client records acceptance of the insurance by telephone or
- Making door-to-door visits to the clients when they are offered the insurance and if the client accepts it, he must fill out an affiliation form. This work is done by a sales force of 25 to 30 insurance agents.

Collection of the premium is made monthly together with the payment of the electricity bill. The clients-insured may make their complaints either to Codensa or directly to the Mapfre insurance company.

The Codensa-Mapfre alliance is currently launching a new campaign, offering three insurances directed at people with low or medium incomes.

Once again it is offering redesigned funeral aid insurances that have an additional coverage for accidental death or homicide. In the case of the traditional funeral aid insurance, the indemnity is US$ 1,800 ($3,600,000) divided in 12 installments of US$ 150 ($300,000); the minimum monthly premium is of US$ 2.4 ($4,850) and the maximum monthly premium US$ 4.7 ($9,450) (depending on the number of persons insured). In the case of the preferential funeral aid insurance, the indemnity is of US $5.000 ($10,000,000) paid in cash; the minimum monthly premium is US$ 3.4 ($6,800) and the maximum US$ 6.7 ($13,400) (depending on the additional services).

They are also offering a personal accident insurance in the case of death or disability.

The personal plan has an insured value between US$ 9,075 ($18,150,000) and US$ 25,575 ($51,150,000); and the monthly premiums fluctuate between US$ 1.4 ($2,750) and US$3.8 ($7,700). The family plan has an insured value between US $11.8 ($23,650,000) and US $ 32,175 ($64,350,000); and the monthly premiums fluctuate between US $ 1.6 ($3,300) and US $4.1 ($8,250). The insured value can be paid in cash, a payment toward the electricity bill or payment of groceries.

It is also offering a life insurance directed toward giving the businessman economic support in the case of death or disability. The premiums fluctuate between US $3.1 ($6,300) and US $12.5 ($25,000); and the amounts insured between US $ 3,150 ($6,300,000) and US $ 12,500 ($25,000,000). The compensation is paid 50% in cash and the difference in 12 monthly installments. Economic aid is also provided for the housekeeping expenses, which fluctuates between US $ 265 ($530,000) and US $1,050 ($2,100,000). (Exchange Rate Approximate: US $ 1 = Colombia $ 2,000)

5.2. Some key regulatory issues to adjust

The Colombian experience shows how developing markets can promote and foster micro-insurance without establishing a specific regulatory framework, it must be noted also that Colombia does not have a specific Insurance Law. However, under this approach some regulatory fragmentation is evident and there are some specific aspects of the regulation that could be adjusted. Particularly, legislation on money laundering tackles some aspects that could be improved. Besides, legislation must analyze if marketing channels are suitable for the special characteristics of microinsurance products.

With respect to marketing channels, there is a regulation that governs only the activities of traditional insurance middlemen (brokers, agents and agency) as were mentioned above. During the workshop about legal relevancy of having to work with insurance agents for the sale of microinsurance, some insurers expressed concerns about a lack of a wider regulation that covers all potential participants in microinsurance distribution activities. Thinking that the products are easy to understand, it seems appropriate to use intensively new chanels in addition to intermediaries (agents and brokers) in the sales of microinsurance, in order to prevent making the product more expensive. According to the profile for the population targeted by microinsurance (people with low income and less education people) it appears to be recommendable for the insurers to use direct distribution channels and to strengthen the diverse client service mechanisms with the goal of accompanying the microinsurance policyholders during the acquisition and use of the insurance. This type of strategy requires the companies to keep the products simple, the microinsurance policies clear and to use low cost distribution channels.

This concern on the part of the different companies with the sales channel takes on greater relevance in the measure that the government created the correspondent banks as a mechanism for improving access to financial services by the poorest income sectors and by people who live in zones that are very remote from urban centers. The services those correspondent banks can offer, however, do not include the sale of insurance. This is one of the specific aspects of the regulation that would have to be reformed since it could be an important channel for mass distribution. The legislation on non-banking correspondents could include the possibility for them to sell insurance, and of course collect premiums, taking special care that the insurance companies that do not belong to financial groups with banking institutions have equal access to those mechanisms.

With respect to the norms on money laundering, from an analysis of the regulation and of opinions picked up in the market, one concludes that although these rules protect the utilization of insurance in money laundering, in the case of microinsurance these rules do not make its development easier. This because microinsurance requires simple sales procedures. The requirement of an in-depth knowledge of the client through filling in a form and holding a personal interview, means asking the possible insured for too much information which will lead to greater costs and the difficulty of obtaining information that poor people do not handle or know. The regulation exempts funeral, accident and health insurance from this obligation; but not life insurance, and property insurances.

5.3. Demand-side overview

In this project the analysis of the demand is one of the most important aspects being analyzed in order to suggest principles for regulating and encouraging micro-insurance. Knowledge of the needs of the possible policyholders, the most important risks that they face, their preferences and knowledge of insurance is considered essential to support the development of the market. These products must effectively minimize the essential risks that both the lower income as well as the medium income sectors must face.

To analyze the behaviour of the potential demand for microinsurance, the results of studies done on this topic in Colombia will first be presented. Secondly, the results of the research done in the context of this study will be presented, which includes focus groups and a survey of micro credit clients of a NGO specialized in micro credit.

5.3.1. Access to insurance products

Significant risk exposure amongst low-income households. The last "Encuesta Nacional de Calidad de Vida, 2003 (National Quality of Life Survey) found that 30.2% of the households in Colombia was affected by an economic loss like unemployment of the head of the household and other members of the family, and the closing of their business, among others. 53% of the households had to decrease their expenditure on apparel and 52% also decreased their expenditures on food. 28.6% of the households had to use their savings and 45.8% requested credit.[30]

There is no regularly information about what kind of credit they used, resources provided by formal financial institutions or other types of providers like relatives and usurers. However, there is evidence that people in low income strata go mainly to informal saving and obtain credit from non banking sources. The Social Survey of Fedesarrollo carried out in 2001 found that 12% of poor people surveyed had credit from relatives, 14% from a non banking lender and 19% from cooperatives.[31]

Significant temporary employment requires flexibility. In Colombia there are no surveys enquiring regularly about access to insurance products, except for a recent special survey executed by Remolina-Estrada/Sönnar Services 2007 for Fasecolda. This survey was applied to persons in strata 2 to 6 (see Box 3) and it found that 45% of the household heads in Colombia are persons who classify themselves as independent, which means that their income is very variable. This lack of stability means that the products offered to them must be flexible so that they will adapt to this characteristic of the Colombian market.

Health and unemployment risk priority. The survey also found that the risks associated to health are comparatively more important for the people in lower strata. In effect, the most important risk, after unemployment, that the persons interviewed in strata 2 to 4 had to face was a serious disease or surgery, while in the strata 5 and 6, the most important risk was associated to a vehicle. The survey also showed that the most common insurance is the funeral insurance, which is held by 40% of those interviewed in stratum 2 and 50% of those interviewed in stratum 3. With regard to knowledge of the products, the survey found that in all the strata those interviewed considered that a voluntary insurance was a basic fundamental need. Nevertheless, 31% of those interviewed in stratum 2 and 24% in stratum 3 considered that insurance is necessary but beyond their reach.

The 2003 Calidad de Vida National Survey of the Dane, the survey on the demand for financial services in Bogotá, 2002 (Dane-Banco Mundial) and the social survey of Fedesarrollo stages III, IV and V (2000 y 2001) have included questions about the use of financial services but not particularly insurance products. However these surveys are very useful to illustrate the access conditions of Colombian people to financial services.

Low access of poor people to financial services. The Dane-Banco Mundial Survey found that an average 39% of the population in Bogotá was using banks. For low income strata that share falls to 22% for people in strata 1 and 2 and rises to 72% for people in strata 5 and 6. These figures are consistent with a low financial deepening indicator (portfolio/GDP) for Colombia. The portfolio/GDP indicator fell in Colombia as a result of the financial crisis at the end of the nineties, but IMF estimations for Colombia account for 23% in 2004, compared with 56% for Chile and 35% for Brazil.

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[30] This survey is applied by the National Department of Statistics and analyzes social and economic conditions in Colombia through a household sample (24.090 households).

[31] See Marulanda *et.al.* (2005).

Different studies have analyzed the reasons for low use of financial services mainly in the poor people group. The main reason is the high costs related with saving accounts and current accounts compared with the profitability. Access to credit is more generalized in mortgage credits. People are less prone to apply for other types of credit, mainly because they have no certainty of future income.[32]

5.3.2. Focus Groups

This study carried out Focus Groups to gain a better understanding of low income people's view on insurance and the risk they face.[33] This tool generates qualitative type results and is a way of investigating the attitudes and perceptions of a group of people about a product or service.

A total of six group sessions were administered, distributed across three cities: Bogotá, Medellín and Barranquilla. Four sessions were held in Bogotá and one session was held in each of the other two cities. Sixty people participated in the focus groups, belonging mainly to income strata 2 and 3. The socio-economic classification corresponds to DANE definitions and operates on a scale from strata 1 (greater needs) to strata 6 (fewer needs)

The groups were made up of equal numbers of workers engaged in the formal and informal sectors. Workers from the informal sector were defined as people who have no access to the social security system, understood mainly as health services and pension savings. Each session included from 6 to 10 participants.

The interviews conducted with the focus group were divided into four topics: i) How people use their money; ii) How they save when they are able to do so, and their perception of unexpected events; iii) Knowledge of insurance and perception of people who acquire it; and iv) Proposals and suggestions about products they would like to find on the market.

The average income of the participants in the focus group was approximately US $400 per month, ranging widely from people who receive US$ 150 to a few people who receive almost US$ 1,200. In the year 2007 the legal minimum monthly wage is US$ 218.

5.3.2.1. Main results of focus group analysis

On the four topics discussed in the interviews, we can reach the following conclusions:

Topic 1. Use of Money

Objective: To find out how regular the income of the interviewees is, how they use their money, and how they save when they are able to do so. The specific objective was to determine the possibility of having sufficient resources to buy microinsurance.

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[32] See Marulanda Consultores (2004).

[33] The discussion guide and transcripts (both in Spanish) are available on request.

- As expected, workers in the informal sector indicated that their income is variable over time.

- The majority of the interviewees mentioned that paying public utilities is a very important item in the family's total expenses, in addition to expenses related to food, health, education, and transportation.

- It was seen that it is normal to borrow from family members, friends, and even sometimes use credit cards.

- For the majority of those interviewed, it is not common to have extra resources to be able to save. Many even commented that at times they do not have enough money to cover the basic needs of their family.

- The few people, who said they have savings, usually save cash in their homes to have in case of an emergency.

- People employed in companies expressed that they have the opportunity to save in an employee fund.

- It was detected that it is common for these people to join informal savings systems called chains or pyramids, but none of the participants said their experience with those systems was negative. The amounts allocated monthly to those types of savings plans were between US$ 10 and US$ 15.

Topic 2. Savings and unexpected events

Objective: To find out what type of events the participants consider unexpected events, which of those events worry them the most, and, in their opinion, have the worst financial consequences. Also, to gather information on the mechanisms used by those interviewed to face those unexpected events.

- It was common to find that the interviewees save in order to cover year-end expenses, such as clothing for their children, school supplies for the new school year, and recreation.

- Few people mentioned emergencies such as accidents or illness as an unexpected event for which it would be good to save. It was necessary to explicitly mention the issue of catastrophic events for them to talk about them.

- All the participants see death, funeral expenses, accidents, illness, hospitalization, disability, natural catastrophes, and their own or a family member's unemployment as unexpected events.

- All the groups state that the unexpected event that most worries them is the death of a family member or their own death when they are the head of household.

- What worries them about that situation is that, if it were to happen, the family would be financially vulnerable. In addition, if someone in the family dies, an immediate concern is how to cover the costs of the funeral, because they are aware that funerals are costly.

- Several of the people interviewed expressed that when unexpected events occur they go to their family, boss, or close friends to cover the expenses produced by the event.

- In all the groups mention was made that the way to protect a family from the loss of the head of household or any other member of the family is by taking out insurance.

- In addition, all those interviewed mentioned the importance of protecting their material goods by insuring them, but no one had an asset insurance. Especially those who are business owners know that they should protect themselves against any loss, damage, or theft.

Topic 3. Knowledge of insurance and perception of people who acquire it

Objective: to find out about the interviewees' experience with insurance, both those who have had insurance and those who have never taken out a policy. For those who have had insurance, an attempt was made to understand their concept of insurance, the risks covered, how insurance was acquired, the way claims were made, if there were claims filed, and their experience with the claim. For those who have not had insurance, an attempt was made to find out if they are familiar with these products, if they think it is good to have insurance, if they think it is expensive, if they find it difficult to understand and purchase, and their degree of confidence in insurance companies.

For those who have been at one time insured, some of them currently insured, the most interesting results are:

- The interviewees indicated that they understand what an insurance policy is.

- They understand that insurance is a form of protection that gives them peace of mind, a backup system, and support. They perceive it as an investment that allows them to think about the future and sometimes prevent an unexpected event, providing stability for the family. They also indicated that insurance protects property in case of an emergency.

- It can be concluded, however, from the testimonies, that there is some confusion about the insurance concept. Savings are confused with insurance. For example, they talked about a vacation insurance that guarantees their vacations at the end of the year by making a monthly payment.

- It is also hard for them to understand that they cannot collect on an insurance policy if nothing happens to them, and they reject the idea that the insurance might not cover 100%.

- The majority has funeral insurance through the electrical utility company CODENSA and the company GAS NATURAL. The two main reasons they were motivated to take out this insurance were ease of payment, and a premium set at a reasonable rate according to their capacity to pay.

- The interviewees indicated that they took out the insurance because the salesperson went to them and because they were pleased to find out that it was easy to acquire the product and make a monthly payment using their utility bill.

- The interviewees said they know that CODENSA and GAS NATURAL are intermediaries between them and an insurer. They trust that the insurer is reliable and guaranteed. In general, they perceive insurance companies as solid and reliable.

- They told of positive and negative experiences with the funeral service provided. Despite the negative experiences, they feel confident about acquiring this type of insurance. They stated, however, that they are not fully familiar with the terms for that type of insurance.

For those who have not been insured, the most interesting results are:

- A minority of those interviewed said they had never been insured. The main reason for not having insurance was not believing it to be necessary. They said they are confident people who do not think about what could happen in the future.

- Some people do not take out insurance because they perceive it to be expensive and they believe only people with larger incomes or in high income strata can buy insurance. As an example they say business people or people working in transportation (public transportation and truck drivers) might purchase insurance.

Topic 4. Proposals and suggestions for products they would like to find on the market

Objective: To find out about the coverage desired by those interviewed according to their needs, the best payment method, and the most convenient payment period.

- In all the sessions the groups stated that to be able to take out insurance it must be economic – accessible – and cover 100% of costs.

- They would like for the insurance companies to explain things to them well so that they can fully understand the coverage offered.

- They hope the agents will be capable people who will be ready to answer all the questions the clients want to ask. They also hope the insurance companies will motivate them using incentives.

- They would like the premiums to match their ability to pay and the payment method to be easy.

- They mentioned several options for how they would like to make the payment. Some prefer it to be debited from their savings accounts – the majority of them have such an account – and others would like to pay in offices close to their neighborhood.

- Among the insurance policies they would most like to see on the market, they mentioned, in order of importance: unemployment, health (including AIDS, heart disease, and infertility), education, life, disability, and home insurance. Some also suggested insurance to protect their assets such as appliances in their home or business, since they are aware that a theft will cause an extra expenditure that they sometimes cannot cover. Some also suggested insurance for vehicles (motorcycles).

- Those interviewed mentioned that to purchase insurance they would like the clauses of the policies to be clear and not cause confusion, and to avoid "fine print." They would like the companies to demonstrate, through testimonies, that they have come through for their clients and that there are no periods when the company is unresponsive. They want strong advertising to convince them that the product is good. They repeated that the salespersons should be skilled and trained. And that the insurance companies go to people's homes to sell the insurance.

- In response to the question of how much they would be willing to pay monthly for an insurance policy, the responses ranged from US$ 7.50 to US$ 15. This amount is greater than the premiums of many of the microinsurance plans offered on the market. Several people were even surprised to hear that monthly premiums exist of US$ 1.50. The value of the monthly premium that they said they could pay reflects, on one hand, their perception that insurance is expensive, and, on the other hand, is in line with the amounts that they say they set aside for informal savings systems such as chains or pyramids.

5.3.3. Survey applied to the clients of a NGO specialized in micro credit[34]

With the goal of complementing the analysis of the focus groups a brief interview was administered to 60 clients at Oportunidad Latinoamérica Colombia (OLC). OLC is a nonprofit non-government organization (NGO) that operates under the auspices of Opportunity International and develops financial and training programs to support people in poverty and, particularly, displaced people by violence. The majority of OLC's clients belongs to income strata 1, are engaged in informal activities, and receive micro loans starting at US$ 300 with a four-month repayment term.

This group of people is a successful example of linking the poorest population group with financial services, including insurance. In general, their first contact with the financial sector comes through OLC, where they are trained in areas related to business management, and they are made familiar with the benefits of insurance. For that reason those interviewed demonstrated knowledge of insurance, confidence in insurance companies, and the ability to pay premiums through a financial institution. It is noteworthy that they showed a stronger preference for protecting themselves from a fire in their home than for insuring the life of the head of household who generates the income. This is due to the fact that the people involved in OLC are located in the poorest areas of the city that are characterized by very precarious housing, and, in addition, many of them have their business in their home.

The results from the questions were:

1. Do you understand what an insurance policy is?

92% said they understand what an insurance policy is.

2. Do you trust insurance companies?

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[34] Data is available on request.

70% said they trust insurance companies

3. If you didn’t have a loan through OLC would you buy insurance?

63% indicated that if they did not have a loan through OLC that requires them to purchase insurance they would still take out a policy.

4. From what contingent loss would you like to protect yourself? Options:

a) Home fire insurance: 83% responded that they want to protect themselves from risk of fire
b) Death of head of household: 75% responded they want to protect themselves from the death of the head of household
c) Disability of head of household: 72% responded they want to protect themselves from the possibility of disability
d) Damage to working tools: 65% responded they want to protect themselves from damage to their working tools

The preference for home fire protection is due to the fact that the population group involved in OLC is located in the poorest areas of the city that are characterized by very precarious housing and, in addition, many of them have their businesses in their homes. An open question, however, produced the results that 25% of those surveyed would like to have health insurance, and 13% education insurance.

5. Mention another contingent loss against which you would like to protect yourself.

Health and education were the most important contingent losses mentioned.

6. Do you have the ability to pay through a financial institution?

68% of those surveyed expressed they could pay premiums through a financial institution.

In conclusion, the focus group methodology made evident the interest on the part of those interviewed in having protection against unemployment, health (including AIDS), and the death of the head of household, as well as guaranties for education. Relative to life insurance, there was interest in life insurance that would reimburse part of what these people feel they have invested, especially if the contingent loss does not occur. This aspiration can be interpreted as a demand for very simple “variable” or “flexible” life insurance. Also, and as was to be expected, the need to educate the insured was detected with respect to the nature and characteristics of insurance products. The interviews also demonstrated the importance informal savings plans called chains or pyramids have in low-income population groups. Despite the fact that they are informal plans, those interviewed did not express knowing of or having had negative experiences with that type of savings plan, and they value them as an easy way to save for a specific purpose.

People seem trust insurers and there is no significant evidence of abuse, which may cause the regulator to consider more onerous consumer protection regulation. In addition, people noted that they appreciated being sold the products, which means that intermediaries using sales people will be preferable.

The survey of poor people who have received micro loans through a NGO showed the important role these institutions have in preparing people who have traditionally been excluded from access to financial services to make use of this type of service. This survey demonstrated that a high percentage of those surveyed believed it important to have an insurance policy, even after they are no longer clients of the MFI. In addition, this group of people expressed a preference for fire insurance, which is explained by the precarious condition of their housing and because in general their businesses operate out of their home.

6. Summary and conclusions

This document provided an overview of the microinsurance market, its evolution and regulatory framework in Colombia in order to identify the core drivers of the development and current state of the market.

The document has six sections, including the analytical framework and introduction:

- **Section 3** provided an overview of the Colombian economic and insurance context.

- **Section 4** described the insurance regulatory framework with the aim of analysing the main aspects affecting microinsurance development.

- **Section 5** then went on to sketch the microinsurance market, considering in turn providers, characteristics of microinsurance products, marketing and distribution channels. An overview of the demand for microinsurance, as gauged from the focus group discussions, was also provided.

- **Section 6** provides the findings and conclusions, stressing key insights and lessons emerging from the Colombian experience.

Key insights emerging from the analysis

Market context. Usage of formal financial services in Colombia is estimated at only 34% of the population and insurance premiums per capita in Colombia are relatively low compared to other Latin American countries. Surprisingly low is the penetration of life insurance, which accounts for only 11% of total premiums. Over the past two decades Colombia has experienced financial liberalisation and growth, but also a major financial sector crisis. Against this backdrop, the country has seen significant microinsurance development, traditionally through its large cooperative insurers and more recently also on the back of microfinance development. This is made all the more remarkable as there is no microinsurance regulation and only indicative financial inclusion policies.

The policy, regulation and supervision context. Under the FLFS, insurance may be provided by either insurance companies or cooperatives. No distinction is made between the two in terms of the regulatory requirements applicable. As a result of the financial crisis of the late nineties regulation and supervision legislation on the solidarity economy sector was strengthened and rules were established for the provision of insurance by cooperatives.

With stronger regulation and supervision, insurance cooperatives have played an important role in the low income market.

The current insurance regulatory framework generally does not hamper microinsurance development. However, there are specific aspects that could be adjusted, such as the anti-money laundering regulation which was stressed as the main barrier for the development of individual microinsurance products. This was addressed by government through the recent imposition of a premium threshold below which KYC requirements do not need to apply.

Salient features of the microinsurance market. In Colombia, microinsurance has grown significantly since around 2005. This has been the result both of the fact that insurers increasingly see a profitable market opportunity in the low-income market as well as of government policy to encourage micro credit and financial inclusion. Given the success of the two large insurance co-operatives, a number of insurance corporations have entered the microinsurance market. By 2007, 18 of the 42 insurance companies in Colombia were offering some type of microinsurance. Insurers have designed products adapted to the needs of the poorest people such as life insurance (including disability cover), insurance tailored to small businesses, insurance for motorbikes and insurance tailored for migrant workers (repatriating insurance). They have also searched for broad-based distribution channels that allow them to get closer to low income people at low cost. Cooperatives and NGOs are the most important microinsurance market channels, almost 40% of microinsurance is sold by these means, followed by public utilities that have been another important channel to reach low income people who are not banked.

Drivers of market development. A number of **market** forces have shaped the development of microinsurance in Colombia:

- *Financial liberalisation enhanced competition*. The increasing competition resulting from the financial liberalisation carried out in the early nineties forced banks and insurance companies to look for new niche markets in the low-income segments.

- *Credit life insurance growth*. The increased competition stimulated microinsurance directly, but also indirectly, through the growth effect on microfinance. The resultant growth in compulsory credit life insurance, driven by banks' strategy to cover their exposure, has also triggered insurers to offer other insurance products through this channel.

- *Demonstration effect by NGOs, MFIs and especially the cooperative sector*. The positive experience of NGOs, MFIs and financial cooperatives further contributed to the emergence of microinsurance and a well developed co-operative system has allowed micro-insurance products to penetrate low-income sectors.

- F*uneral parlours familiarise the public with the concept of insurance cover*. In addition, the funeral parlour sector, while not classified or supervised as insurers, has introduced the low-income market to insurance.

Though the Colombian experience shows that microinsurance can grow even in the absence of dedicated regulation, this has only been possible because insurance **regulation** does not impose an unduly heavy burden on the underwriting or intermediation of microinsurance:

- *Active government encouragement of low-income market activity.* To date one of the main impacts of the Opportunity Banking policy has been the introduction of "non-bank correspondents" as an intermediary category to support the distribution of financial services in poor and remote areas. The expansion of micro-credit in turn paves the way for credit life microinsurance expansion.

- *Demarcation rules favourable to market development.* An insurer is allowed to provide health, non-life and group life policies under a single license.

- *Flexible market conduct regime.* The Colombian regulatory framework facilitates microinsurance intermediation by accommodating new channels within the "direct sales" or "agencies" categories or through specific subordinate legislation as they arise. Furthermore, no commission caps apply to the intermediation process. Cooperatives may sell insurance to non-members and may act directly as distribution channel. Lastly, the FS delegates supervision of agents to insurers. These factors combine to make Colombia one of the sample countries with the most flexible market conduct regime. This gives providers the confidence to pursue distribution innovation, as witnessed in the various new channels emerging.

- *Insurance provided by funeral entities unregulated*. Funeral entities serve a large part of the market and have also supported formal market development by increasing awareness and familiarity with the concept of insurance. They operate on an unregulated and unsupervised basis. Though this "regulatory forbearance" has by and large served the development of the market, it could create the risk of consumer abuse if not carefully monitored by the supervisor.

- *Prudential requirements do not facilitate entry by smaller entities dedicated to microinsurance*. Despite all the positive regulatory drivers, uniform prudential requirements imply that it remains difficult to provide insurance "from the bottom up", as there is no regulatory tier to accommodate the unique low-risk features of microinsurance.

  Key issues for the regulation of microinsurance in Colombia going forward. As stated, the restrictive anti-money laundering requirements have already been lifted for microinsurance. It will furthermore be important for the regulator to rethink the regulation applicable to insurance distribution to the low-income market. For example, the fit and proper and technical qualification requirements of intermediaries can make them a costly channel for the commercialisation of simplified mass market products, highlighting the need to explicitly consider the scope for alternative distribution within regulation (though in practice the intermediation requirements are very flexibly applied by the supervisor). Another area that would need attention is the fact that the permitted actions for correspondent banks (under the Banca de las Oportunidades Policy) do not include the sale of insurance; they could only collect insurance premiums. This is a service that could be included in the legislation in order to strengthen microinsurance distribution channels, especially in very poor urban areas and remote regions.

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Appendix 1: Analytical framework

Financial inclusion framework

The five country studies explored the drivers of financial inclusion within the insurance market, in particular considering the impact of regulation. Ultimately, more inclusive financial systems are the desired outcome of the emerging guidelines proposed in this report.

Financial inclusion is achieved when consumers across the income spectrum in a country can access and sustainably use financial services that are affordable and appropriate to their needs. The overall level of inclusion achieved is determined by a variety of factors affecting the individual directly (demand-side factors) as well as the institutions providing the services (supply-side factors). Figure 5 indicates this schematically:

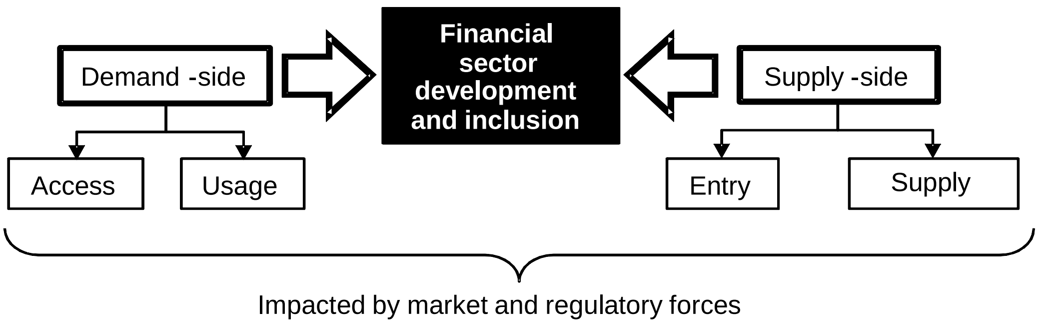

Figure 5. Financial inclusion framework

Source: Da Silva & Chamberlain, 2008

These factors may explicitly exclude individuals from using a particular service (referred to as **access** barriers) or may discourage users from using a particular service even if they are not explicitly excluded (referred to as **usage** barriers). Similarly, impacts may completely exclude or may discourage financial service providers from providing a particular financial service to the lower-income market – termed **entry** and **supply** barriers respectively. These concepts are briefly explained below.

- **Access** barriers consider the factors that make it impossible for a individual to use a particular financial service. The FinMark access methodology35 identifies five factors that impact on access: physical proximity, affordability, eligibility, appropriate product features/terms and regulation.

[35] For more information see the discussion contained in Chamberlain (2005).

- **Usage** focuses on factors that may discourage individuals to take up formal financial services even if they do not present an absolute barrier. Usage decisions involve the exercise of judgment by individuals on the value of the product and its ability to meet their needs based on their experience and knowledge. This judgment is exercised within a complex set of considerations, constraints and priorities. Usage drivers may include: the value proposition of the formal product (e.g. the perception of "throwing money in the water" by paying insurance premiums when you do not necessarily claim); relative cost (e.g. compared to informal alternatives); the "hassle factor" (e.g. of filling out forms); and perceptions of formal products and institutions (e.g. the fear of "officialdom" and the belief that financial institutions are for the rich).

- **Entry** factors include market and regulatory forces that may prevent particular players from operating in the low-income market, or may make it difficult for informal providers to become formal sector players. This may include regulations restricting the type of legal entity that may for example provide insurance.

- Similar to the demand-side, **supply** factors do not explicitly prohibit institutions to enter into the low-income market but may discourage them from doing so. These may for example include proportionately increased regulatory costs on low-value transactions that undermine their already marginal profitability. While not necessarily making it impossible to serve the low-income market, it makes operating in this market unattractive.

The state of financial inclusion in a particular country is a composite of these four factors. The particular question that this project seeks to answer is how **regulation**, propagated through the various drivers of access, usage, entry and supply, impacts the overall level of financial inclusion in the insurance sector.

Goal of microinsurance

The country studies presented in this report accordingly focus on the role that the insurance market can play in reducing the vulnerability of the poor. Why would one want to develop microinsurance markets? The ultimate goal of microinsurance is to enable the poor to mitigate their material risks through the insurance market, in order to reduce vulnerability, thereby increasing their welfare. To be successful, microinsurance should therefore mitigate the most material risks faced by the poor client in a way that is affordable and appropriate to the low-income market.

In the process of mitigating their risk, microinsurance may also stimulate the provision of other services that are important to the poor, for example, credit services, funeral services or health services. This is achieved by providing more predictable income flows to providers that ensure viability of the provision of such services to the low-income market. Therefore microinsurance enhances the welfare of the poor by addressing material risks as well as supporting the delivery of critical services.

It must be noted that the availability or even take-up of insurance *per se* is not sufficient to achieve the goal of reduced vulnerability and improved welfare. To deliver value, low-income insurance products should also be affordable and appropriate to the needs of the poor. This requires sufficient awareness of the availability and value of insurance amongst the poor as well as the ability to claim on policies. Providers and intermediaries should also treat consumers fairly. If it is difficult or impossible for a low-income client to make a legitimate claim on their insurance policy it will not reduce vulnerability and renders the product of little value.

The country evidence discussed in this document shows that microinsurance take-up is often not the result of voluntary strategies by the poor to mitigate their material risks, but is rather the outcome of compulsion by *credit providers* seeking to cover their own exposure to default. In this case, microinsurance may still deliver significant value to the client but care needs to be taken to ensure fair treatment of the low-income consumer.

Definition of microinsurance

Conceptual definition. Microinsurance is defined by the IAIS (2007b) as "*insurance* that is *accessed by [or accessible to*[36]*] the low-income population*, provided by a variety of different entities, but run in accordance with generally accepted insurance practices (which should include the Insurance Core Principles). Importantly, this means that the risk insured under a microinsurance policy is managed based on insurance principles and funded by premiums". It therefore excludes social welfare as well as emergency assistance provided by governments, "as this is not funded by premiums relating to the risk, and benefits are not paid out of a pool of funds that is managed based on insurance and risk principles*"*.

This definition encompasses three concepts that require further explanation in the context of this study: "insurance, "accessible to/accessed by", the "low-income population".

- *Insurance.* Generally, insurance denotes a contract in terms whereby an insurer, in return for a premium, undertakes to provide policy benefits. It is distinguished from e.g. social welfare in that it is funded by premiums relating to the risk, and in that benefits are paid out of a pool of funds that is managed based on insurance and risk principles (IAIS, 2007). Benefits may include one or more sums of money, services or other benefits, including an annuity. Microinsurance forms part of the broader insurance market, distinguished by its particular low-income market segment focus (that often requires distinctive methods of distribution or distinctly structured products).

- *Accessible to*. Microinsurance products need to be accessible and appropriate to the low-income population, i.e. that the low-income population be in a position to sustainably use such products (including claiming).

The low-income population. This study does not propose any specific income cut-off for the microinsurance target market. Instead, the target market should be defined within the local country context. Microinsurance is not strictly limited to those living under the national poverty line or the comparative measures (e.g. $1 or $2 adjusted for purchasing power parity). Many of these households may actually be beyond the reach (e.g. affordability) of an insurance mechanism and will remain the dependent on the social security system.

[36] Authors' own insertion.

Furthermore, generally low income levels means that even the middle-income class (not classified as poor under the national poverty line) in a particular country will have relatively low income levels and, therefore, require low-premium products.

Operational definition. Definitions based on the income levels of the purchaser or the client are difficult and costly to implement in practice. As result, the practical definitions applied by the market or regulator mostly define microinsurance policies by setting benefit or premium limits, thereby ensuring that it is mostly (but not exclusively) targeted at the poor. Other functional criteria used to define microinsurance (virtually always in c*ombination with a bene*fit cap) include the following:

- Product categories that particularly reflect the needs of the poor (e.g. funeral insurance, or insurance for motorcycles or cell phones important to the low-income market for business purposes)

- Distribution channels, especially channels accessible to the poor;

- Simplicity of terms, conditions and processes;

- Contract characteristics, for example limiting exclusions that may be difficult for clients to understand or allowing clients to catch up on occasionally missed premiums without lapsing the policy

The insurance value chain

Delivering an insurance product to a client comprises a number of activities collectively referred to as the insurance value chain. Unlike the transaction banking value chain, where the activities are often performed by the same legal entity, the various activities comprising the insurance value chain are typically performed by more than one legal entity. The risks attached to the various activities differ and they are regulated by different regulators and supervisors or not at all.

Figure 6 presents a picture of the generalised structure of the insurance value chain:

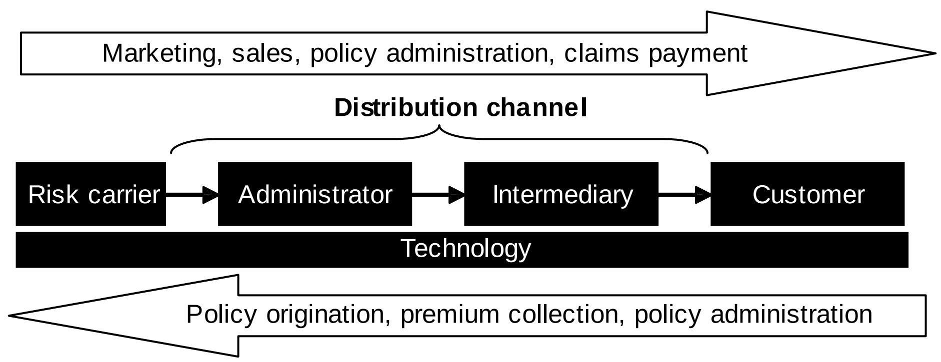

Figure 6. Insurance value chain

Source: Chamberlain, Bester et al, 2006, quoting Leach, FinMark 2005.

The functions of the various components of the insurance value chain are:

- *Underwriting:* This is the responsibility the risk carrier, defined as the entity that in the final instance is liable for the insurance risk. In the formal financial sector, the risk carrier is usually a registered insurer (that may obtain re-insurance) or another entity (such as a cooperative) authorised to provide insurance.

- *Administration:* Administration may be done at the level of risk carrier, intermediary or may even be outsourced to a specialised entity that often does not fall under the jurisdiction of the insurance supervisor. Administrative costs contribute a substantial proportion to overall insurance costs and innovation on this aspect is, therefore, of particular interest for microinsurance.

- *Intermediation:* Intermediation deals with all aspects of client contact and related activities (e.g. product origination) and may take a variety of forms including an insurer's direct sales division, captive or independent agents, retailers, banks and non-bank financial service providers, NGO MFIs, credit cooperatives, etc. Different types of intermediaries may be more or less suited to distribute microinsurance and may also be affected differently by regulation.

- *Technology:* Technology plays a role across the value chain and may include a variety of technologies ranging from sophisticated electronic solutions such as the use of mobile phones to social technologies such as premium collection through self-help groups. The appropriate use of technology may facilitate better risk management as well as lower the costs for microinsurance.

Understanding microinsurance in a particular market therefore requires focusing on more than just insurers and products. Particular attention has been paid to the intermediation of insurance in the markets reviewed in order to understand the regulatory ramifications on each part of the value chain. This is especially true for emerging technologies and innovations (for example mobile phone payments, distribution through retailers, etc.).

The distinction between formal and informal

Throughout this document, reference is made to informal and formal (or regulated and unregulated) markets, products, providers or distribution channels. Key issues to consider include the reasons for informality and what the appropriate policy and regulatory response should be. It is therefore important to clarify upfront what is implied by informality:

Formal. Formal financial products and services are defined as products or services provided by financial service providers[37] that are registered with a public authority in order to provide such services[38].

[37] In turn defined broadly as any provider of financial services – in this instance insurance.

Informal. Informal financial services, therefore, refers to everything that is not formal as defined above and includes a wide range of providers. At its simplest this includes completely informal societies that are often of a community and mutual nature. In some cases informal markets may also include formal legal entities (e.g. funeral parlours) providing insurance without being regulated for the purposes of doing so. Informal insurance is not necessarily illegal. Specific providers or products may be exempted from insurance regulation or may simply be operating in the absence of regulation. Where a particular section of the formal market is regulated in theory but not supervised in practice, it may actually present similar risk and challenges to the informal sector.

The informal financial sector can play a critical role in financial sector development. The existence of large informal markets can be a key indication of demand for insurance products not met by the formal market as well as potential barriers to formalisation and market development. Informal institutions often fill the vacuum created in the process of formalisation by acting as distribution mechanism or providing the service themselves. The scale and number of informal insurance providers may provide a reality check on the challenges facing supervisors and regulation that attempts to formalise these markets. In many cases, the supervision of this sector may simply fall beyond the logistical or resource capacity of the supervisor.

From an inclusion perspective, the objective is to facilitate the development of the formal sector and encourage formalisation while at the same time preserving the critical services provided by the informal sector.

Categories of risk

The definition and analysis of risk and its various drivers is central to the analysis and proposals contained in this document. In this section we note the definitions and concepts that are applied in the discussion of risk.

The Insurance Core Principles (ICPs - IAIS, 2003) hold that "the supervisory authority requires insurers to recognise the range of risks that they face and to assess and manage them effectively" (ICP 18) and to "evaluate and manage the risks that they underwrite, in particular through reinsurance, and to have the tools to establish an adequate level of premiums" (ICP 19). ICP 18 states that the insurance supervisor plays a critical role by reviewing the insurer's risk management controls and monitoring systems and by developing prudential requirements to contain these risks. In the final instance, it is the responsibility of the board (via good corporate governance practices) to ensure that risk is adequately managed.

The risk of insurance business stems from a variety of reasons. To simplify the discussion in this document we distinguish three (interdependent) categories of risks: prudential risk, market conduct risk[39] and supervisory risk:

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[38] This is the definition generally applied by the World Bank.
[39] These categories as are in line with the solvency methodologies as outlined in IAA (2004) and IAIS (2007a).

- *Prudential risk* refers to the risk that the insurer is unable to meet its obligations under an insurance contract. Insurance provides benefits on a defined risk event in return for premiums that are paid in advance. A contractual commitment to provide benefits create the risk that the insurer's liabilities in respect of expected future claims at some point in time may exceed the assets they have available to meet those claims. This is driven by a number of more specific risks categorised by the International Actuarial Association as underwriting risk, credit risk, market risk, operational risk and liquidity risk (IAA, 2004). Prudential risk is in the first instance determined by the nature of the insurance products in an insurance portfolio (underwriting risk determined by the likelihood and size of exposure) and secondly by how the insurer is managing and providing for its obligations under these policies. Key features of the insurance product that impact on risk are: the nature of the risk event covered and its expected frequency and impact; the duration of the product contract; the benefit value; product complexity of the product. The product-driven nature of underwriting risk is a key feature of risk that we return to later in this document.

- *Market conduct risk*[40] refers to the risk that the client is not treated fairly and/or the does not receive a payout on a valid claim. Effectively this is the risk that clients will be sold products that they do not understand, are not appropriate to their needs, and/or will not be able to claim on. This risk is driven by various factors including: the nature of the product (e.g. product complexity, level of cover provided), the nature of the intermediation process (e.g. compulsory/voluntary nature of the purchase, standalone/embedded nature of the product, the level of disclosure or advice, nature of the claims process) and the nature of the client (e.g. level of sophistication and financial literacy). In some insurance literature market conduct risk may also refer to the risk arising from the insufficient disclosure of financial information by the insurer to investors and supervisors. This is **not** included in the definition of market conduct applied in this document.

- *Supervisory risk* refers to the risk that the supervisor is unable to sufficiently supervise (due to limited capacity) specific components of the market. The result of this is that an insurer or insurance product with low technical/underwriting risk may actually turn out to have a high risk to the system because it is not appropriately supervised.

Policy, regulation and supervision

<u>Regulatory vs. non-regulatory drivers of market development</u>

This report is about the impact of regulation on the development of microinsurance markets. Many insurance markets initially developed in an unregulated environment. The first pitfall to guard against is therefore to think that markets develop as a result of regulation. Largely they do not. The insurance sector is impacted by external factors in the financial sector and by the economic and country context more broadly, such as the macro-economic environment, the political economy, the general and financial sector

[40] Market conduct concerns may impact on prudential risk in that the reputational damage may, e.g., lead to an insurer becoming insolvent but it is still quite distinct from it.

infrastructure, and the demographic profile of the country (gender, age, income levels and the distribution of income). For example, a country undergoing financial liberalisation or recovering from a financial sector crisis or recession will face different policy challenges impacting on its insurance regulatory framework than other countries. Likewise, a country where the majority of the population is poor, or where the financial sector and other infrastructure is poorly developed, will face different circumstances and goals than other countries.

The first challenge is therefore to distinguish between the regulatory and non-regulatory drivers of market development. Whereas this distinction is quite clear in certain cases, causality is often a matter of degree and even opinion. The approach followed in this study is to identify the non-regulatory drivers of market development at a high level to provide the general context for tracing the impact of regulation. As far as possible we identify all the potential impacts of regulation, even though in many cases regulatory drivers may have been overridden by other market factors.

Purpose of insurance regulation

It is important to note that regulation is not an end-goal in itself, but is the means to ensure the existence and development of a well-functioning market. A well-functioning market includes serving the broadest possible client base, including the poor. In seeking to achieve the goal of a well-functioning market policymakers, regulators and supervisors pursue a number of more specific objectives including:

- *Stability of the sector*. This objective is sought by ensuring the soundness of operators and may resonate in capital requirements, corporate governance requirements, fit and proper requirements and other aspects of the regulatory framework. Among the regulatory objectives, this is often the one that has been pursued for the longest time.

- *Consumer protection*. While this is also an implicit goal in the stability objective, this objective most often resonates in market conduct/intermediation regulation (both in terms of the intermediation channels permitted, the due process to be followed, the commissions that can be charged and the requirements placed on the intermediaries themselves).

- *Improving market efficiency*. This may entail preventing anti-competitive behaviour and overcoming information asymmetries. In its application such regulation may overlap with both stability and market conduct regulation.

- *Market development* (or financial inclusion more specifically) is sometimes included as an explicit policy or regulatory/supervisory objective – for example in India, where the supervisor (IRDA) is also explicitly tasked with a development mandate.

- *Other strategic objectives*. This can for example include the prevention and control of financial crime as required by international standards imposed by the Financial Action Task Force or the economic empowerment of previously disadvantaged citizens as is the case in South Africa.

Given the ultimate goal, none of these individual objectives should be pursued at the cost of a well-functioning market. Some objectives may also conflict. For example: where an authority has the explicit mandate to develop the market, this may require the relaxation of regulations imposed for stability purposes. Therefore the market development objective may clash with the way the stability objective was pursued. Often, various objectives however mutually enhance one another.

Public policy instruments

To achieve its stated objective, a government uses three categories of public policy instruments to influence markets:

- *Policy*. The term "policy" denotes the declared intention of a government on how it wishes to order the financial sector and the objectives that it wishes to achieve. The trade-offs between various government objectives (for example consumer protection and financial inclusion) is therefore managed within the policy domain. Such policy can be contained in a specific policy document (i.e. can comprise a dedicated policy framework), but can also be the stated intention of government more broadly/generally, be contained in speeches, in the preamble to legislation and in other documents (i.e. the general policy stance). Policy may sometimes be sufficient, in itself, to achieve government objectives even without regulation following from the policy. This may be the case particularly where government wants the market to achieve the stated goals. In most instances, however, policy is the canvas against which *regulation* is then developed.

- *Regulation*. Technically speaking, the statutes of a country are termed *legislation*. It is passed by the national legislative authority (be it parliament or congress). Legislation represents a relatively rigid public policy tool that is normally difficult and time consuming to pass and difficult to amend. In addition to legislation, *subordinate legislation* may be issued by the executive authority or regulator. Such instruments are more flexible, yet still have the force of law. In the event of conflicts, legislation will take precedence. In some jurisdictions, subordinate legislation is referred to as *regulations*. When referring to regulation, this document bestows a broader meaning on the term than subordinate legislation, namely: the various legal instruments with binding legal powers (legislation as well as subordinate legislation) that together comprise the regulatory body or regulatory framework pertaining to insurance. Regulation furthermore includes the action of regulating the insurance industry to achieve the policy goals. This in turn includes the development of *regulatory* requirements. The regulator may issue *guidance* in relation to regulation. Such guidance can be in the form of memoranda or circulars. It does not have the force of law, but can be converted into legally binding regulations if required.

- *Supervision*. Supervision describes the functions whereby the state seeks to ensure compliance with regulation. The supervisor's role can therefore be defined as the oversight and compliance, on behalf of the state, of the implementation of regulation by private entities, with the power to impose the penalties allowed for in regulation if not adhered to.

Generally, the policymaker will be the national government or the ministry with jurisdiction over the insurance industry, the regulator will be the ministry issuing the legislation pertaining to insurance or a statutory body issuing subsidiary rules, and the supervisor will be a statutory body for implementing such regulation, e.g. an insurance commission or financial services board, superintendence or authority more broadly. In many jurisdictions the supervisor as defined here can therefore simultaneously be the regulator.

Insurance regulatory scheme

Different categories of regulation are used to influence the behaviour of participants in the insurance value chain. These are collectively referred to as the insurance regulatory scheme, which can be captured in the diagram below. The report uses this scheme to analyse the impact of policy and regulation on the development of microinsurance markets in the sample countries.

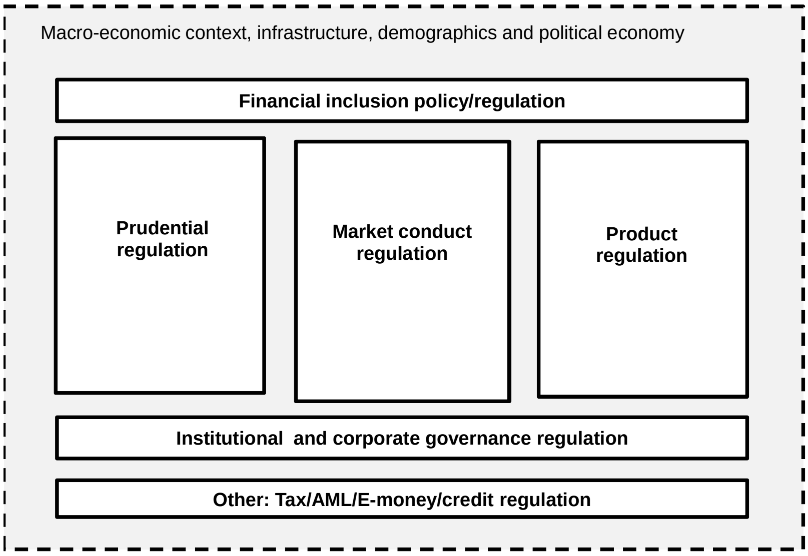

Figure 7. The insurance regulatory scheme

Source: authors

Financial inclusion policy/regulation refers to policy or regulation promulgated with the objective of extending access to and usage of formal financial services by persons who are either excluded from or who do not use formal financial services (provided by registered/licensed and supervised financial institutions). Such regulation can take various forms, for example compulsory or consensual quotas targeting defined population segments, financial literacy provisions, tax incentives, extending the reach of the formal payment system, etc. Sometimes a government may choose not to regulate financial inclusion, but simply to adopt financial inclusion policies with the explicit aim that financial institutions would pursue inclusion on a voluntary basis. Although these do not have the force of law, they will directly impact the conduct of providers.

Prudential regulation seeks to ensure that insurers are able to meet their contractual obligations to their clients. This is done by, for example, setting minimum entry requirements such as minimum levels of capital and requiring compliance with a set of prudential regulations governing the functioning of the insurer.

Market conduct regulation refers to the regulation of the distribution or intermediation of insurance products. Regulation of this kind could include requirements as to who can intermediate insurance, fit and proper requirements for agents and brokers and other intermediaries, regulation of the selling process, including disclosure requirements and giving of advice, regulation of the payment of commission, statutory requirements that make the take-up of certain types of insurance compulsory (for example credit life insurance may be declared compulsory when taking out a non-collateralised loan), etc.

Product regulation can be distinguished from prudential and market conduct regulation in that it does not relate to the insurer or the sales/intermediation process, but rather to the product in question. While provisions relating to product regulation are usually contained within either prudential, institutional or market conduct legislation, it therefore represents a distinct regulatory angle. Product regulation aims to ensure stability and consumer protection by regulating the nature and structure of insurance products. In the most basic form, regulatory systems are often structured around definitions of specific products or product categories.

Box 7. Aspects of product regulation.

Product regulation may involve one or more of the following:

- *Registration/ approval*. In some jurisdictions, regulation stipulates that products need to be filed with the regulator/supervisor, with a window period for response by the supervisor, before the product is launched. If no objection is made by the supervisor within the stipulated time frame, the product is automatically approved. In other instances, explicit approval is required by the regulator before products may be offered. This may be used as a means of compensating for an otherwise light regulatory burden and to allow innovation.
- *Standards*. Regulation may require microinsurance to meet specific standards on simplification, standardisation, documentation, cool-off periods, term, exclusions, etc. In some instances, requirements relating to terms and provisions may be quite onerous; in others it may facilitate innovation.
- *Price control*. Regulation may set specific minimum or maximum prices for product categories. Premium floors are mostly aimed at trying to ensure solvency of the insurer by avoiding price competition, whereas premium ceilings are mostly motivated by consumer protection considerations (though in practice they often serve to protect insurers against intermediaries with bargaining power, rather than protecting the consumer.
- *Demarcation*. Regulation may also prohibit the provision of insurance products by particular players (e.g. non-corporates) or may determine that certain types of products may only be provided by certain types of providers (demarcation).Creating a product-based approach to microinsurance where a regulatory space is created for those who can comply with product standards is therefore a further instance of product regulation. The intention is to limit the risk, thereby justifying different market conduct and prudential standards.
- *Compulsory products*. Lastly, regulation may compel insurers to offer specific products.

Institutional regulation, which includes corporate governance regulation, refers to those statutory requirements that determine the legal forms or persons, for example public companies and cooperatives that can underwrite insurance, as well as the regulatory corporate governance requirements applicable to these legal forms. The nature and extent of the corporate governance requirements normally determine whether that particular legal institution is suitable to manage the risks inherent in underwriting insurance. The institutional and corporate governance regulation is generally not specific to the insurance sector (although some countries have a tradition of passing specific statutes for individual insurance firms, especially mutuals), but generic across sectors.

Other regulation. A number of other regulatory requirements could also impact the development of the microinsurance market. Although not insurance-specific, they impact the underwriting and intermediation of insurance products. Examples include anti-money laundering provisions, taxation, regulation of the payment system (that impacts the ease whereby premiums can be paid), regulation of the microfinance sector and credit regulation generally.

It is not only regulation *per se* that impacts market developments. The absence of regulation can play an equally powerful role. Similarly, even if regulation exists, a supervisory approach of “benign neglect” or “forbearance” can allow the market to develop in ways that cannot be foreseen ex ante by a regulator.

Appendix 2: Portfolio composition of life insurance

Portfolio composition of life insurance (US$ millions)

Line of Business	Code	Premmium 2005	Line of Business's Share (%)	Premmium 2006	Line of Business's Share (%)
Life Group	30	219	20.5%	271	20.7%
Individual Life	33	122	11.4%	133	10.1%
Health	31	127	11.9%	145	11.0%
Personal Accidents	27	47	4.4%	56	4.2%
Education	29	43	4.0%	45	3.5%
Voluntary Annuities	37	22	2.0%	30	2.3%
Disease of high cost	32	14	1.3%	11	0.9%
Funerals	26	5	0.5%	8	0.6%
Pensiones con conmutación personal?	38	5	0.4%	80	6.1%
Life Collective	28	1	0.1%	1	0.1%
Total		1,069	100.0%	1,312	100.0%

(*)Source: data extracted from official webside of Financial Superintendence

Exchange Rates: US$ 1 = Colombia Pesos 2,320.8 (2005); Colombia Pesos 2,358.0 (2006)

Portfolio composition of non life insurance (US$ millions)

Line of Business	Code	Premmium 2005	Line of Business's Share (%)	Premmium 2006	Line of Business's Share (%)
Fire and Earthquake	7 y 8	271	15.8%	271	14.3%
SOAT (*1)	4	198	11.6%	239	12.6%
Engineering	15,11,12,18	122	7.1%	121	6.4%
General Civil Liability	6	105	6.1%	117	6.2%
Guarantee (Surety)	5	103	6.0%	125	6.6%
Transport	10	92	5.4%	92	4.9%
Life Group*	30	83	4.9%	80	4.2%
Robbery	9	46	2.7%	67	3.5%
Vehicle	13	44	2.6%	45	2.4%
Aviation	16	39	2.3%	34	1.8%
Personal Accidents*	27	25	1.5%	29	1.6%
Funerals*	26	20	1.2%	22	1.1%
Loss of Revenue	14	16	0.9%	16	0.9%
Home	25	15	0.9%	17	0.9%
Health Insurance*	31	12	0.7%	12	0.6%
Life Collective*	28	8	0.5%	12	0.6%
Desease of higth cost*	32	3	0.2%	3	0.2%
Others		13	0.7%	17	0.9%
Total		1,712	100.0%	1,892	100.0%

Source: data extracted from official webside of Financial Superintendance

(*1) SOAT (Transit Accident Compulsory Insurance)

Exchange Rates: US$ 1 = Colombia Pesos 2,320.8 (2005); Colombia Pesos 2,358.0 (2006)

Appendix 3: Portfolio composition of non-life insurance

Appendix 4: Written life premiums

Written Life Primium (US$ millions)

	Life Insurance Entities	2005	Share of Life Market	2006	Share of Life Market
1	Compañía Suramericana de Seguros de Vida	245	22.9%	346	26.4%
2	Compañía de Seguros Bolivar	171	16.0%	184	14.0%
3	Vidaalfa	90	8.4%	115	8.7%
4	Aseguradora de Vida Colseguros	74	6.9%	87	6.6%
5	Compañía Suratep	68	6.4%	82	6.3%
6	Seguros de Vida Colpatria	63	5.9%	74	5.6%
7	BBVA Seguros de Vida	47	4.4%	60	4.6%
8	Compañía Agrícola de Seguros de Vida	46	4.3%	51	3.9%
9	Riesgos Profesionales Colmena	46	4.3%	50	3.8%
10	Royal & Sun Alliance Seguros de Vida	43	4.0%	39	2.9%
11	Mapfre Colombia Vida Seguros	39	3.6%	53	4.0%
12	Liberty Seguros de Vida	35	3.3%	45	3.4%
13	AIG Vida	22	2.1%	35	2.6%
14	Skandia Compañía de Seguros de Vida	19	1.7%	25	1.9%
15	**La Equidad Vida (Cooperativa)**	17	**1.6%**	20	**1.5%**
16	Previsora Vida	14	1.3%	15	1.1%
17	Compañía de Seguros de Vida Aurora	12	1.1%	11	0.8%
18	Seguros de Vida del Estado	11	1.0%	13	1.0%
19	Generali Colombia Vida	5	0.5%	5	0.4%
20	Pan American de Colombia	3	0.3%	3	0.2%
	Total	1,069	100.0%	1,312	100.0%

Sourse: Financial Superintendence.Exchange Rates: US$ 1 = Colombia Pesos 2,320.8 (2005); Colombia Pesos 2,358 (2006)

Appendix 5: Written non-life premium

Written Non-Life Primiums (US$ millions)

	Non-Life Insurance Entities	2005	Share of Non-Life Market	2006	Share of Non-Life Market
1	Liberty Seguros	202	11.8%	230	12.1%
2	Aseguradora Colseguros	183	10.7%	173	9.2%
3	Compañía Suramericana de Seguros	163	9.5%	176	9.3%
4	La Previsora (Estatal)	158	9.2%	170	9.0%
5	Seguros del Estado	155	9.1%	155	8.2%
6	Compañía Agrícola de Seguros	133	7.8%	162	8.5%
7	Seguros Comerciales Bolívar	105	6.1%	115	6.1%
8	**Aseguradora Solidaria (cooperative)**	**75**	**4.4%**	**86**	**4.5%**
9	QBE Central de Seguros	74	4.3%	93	4.9%
10	Mapfre Seguros Generales	68	4.0%	80	4.2%
11	Royal & Sun Alliance Seguros	64	3.7%	70	3.7%
12	Seguros Colpatria	63	3.7%	70	3.7%
13	AIG Colombia Seguros Generales	59	3.4%	60	3.2%
14	ACE Seguros	36	2.1%	44	2.3%
15	CHUBB de Colombia Compañía de Seguros	36	2.1%	38	2.0%
16	Compañía Mundial de Seguros	29	1.7%	40	2.1%
17	Generali Colombia Seguros Generales	27	1.6%	28	1.5%
18	Compañía Aseguradora de Fianzas Confianza	23	1.3%	28	1.5%
19	BBVA Seguros	14	0.8%	16	0.9%
20	Seguros Alfa	13	0.8%	11	0.6%
21	**La Equidad Generales (cooperative)**	**13**	**0.8%**	**18**	**1.0%**
22	Condor Compañía de Seguros Generales	10	0.6%	13	0.7%
23	Mapfre Seguros de Crédito	5	0.3%	7	0.4%
24	Seguroexpo de Colombia (Crédito y Comercio Exterior)	5	0.3%	7	0.4%
	Total	1,712	100.0%	1,892	100.0%

Source: Financial Superintendence. Exchange Rates: US$ 1 = Colombia Pesos 2,320.8 (2005); Colombia Pesos 2,358.0 (2006)

Appendix 6: Commercial banks

Authorized Commercial Banks

Code	
1-1	Banco de Bogotá
1-2	Banco Popular S.A.
1-6	Banco Santander Colombia S.A.-Banco Santander-
1-7	Bancolombia S.A. o Banco de Colombia
1-8	ABN Amro Bank (Colombia) S.A. - ABN Amro Bank-
1-9	Citibank-Colombia S.A.
1-10	Banistmo Colombia S.A. (BANISTMO)
1-12	Banco GNB Sudameris Colombia (SUDAMERIS)
1-13	Banco Bilbao Vizcaya Argentaria Colombia S.A.
1-14	Banco de Crédito de Colombia S.A.
1-23	Banco de Occidente
1-30	Banco Caja Social BCSC
1-39	Banco Davivienda S.A.
1-42	Banco Colpatria Red Multibanca Colpatria S.A.
1-43	Banco Agrario de Colombia (Banagrario)
1-44	Banco de Crédito y Desarrollo Social - Megabanco S.A.-
1-49	Banco Comercial AV Villas S.A.(Banco de Ahorro y Vivienda AV Villas)
1-50	Granbanco S.A. (BANCAFÉ)

Source: Financial Superintendence.

Appendix 7: Commercial finance companies

Code	
4-5	Financiera América S.A. CFC (Finamérica CFC)
4-8	Giros & Finanzas CFC S.A.
4-13	Inversora Pichincha S.A. CFC
4-17	Comercia S.A. CFC
4-22	Confinanciera CFC
4-23	Servicios Financieros S.A. Serfinansa CFC
4-24	Financiera Andina S.A. Finandina CFC
4-26	Compañía de Financiamiento Comercial Sufinanciamiento S.A. CFC
4-31	G.M.A.C.Financiera de Colombia S.A. CFC
4-33	Financiera Internacional S.A. CFC
4-35	Macrofinanciera S.A. CFC
4-46	Coltefinanciera S.A. CFC
4-59	Corficolombiana Leasing S.A. CFC
4-65	Leasing Bolívar S.A. CFC
4-67	Leasing Colombia S.A. CFC
4-74	Leasing Citibank S.A. CFC
4-84	Leasing Bogotá S.A. CFC
4-87	Leasing de Crédito S.A. Helm CFC
4-90	Leasing de Occidente S.A. CFC
4-97	Leasing Popular CFC
4-101	Leasing Bancoldex S.A. CFC
4-102	Financiera Compartir S.A. CFC
4-108	Dann Regional S.A. CFC
4-110	CMR Falabella S.A. CFC.

Source: Financial Superintendence

Appendix 8: The fundamental law of the financial system (FLFS), (Decree 663, 1993).

First Part "Basic description of the entities submitted to the supervision of the Financial Superintendence"

This part contains thirteen chapters and the followings four are linked with insurance.

Chapter I Financial System Structure

Establishes that the insurance entities, insurance intermediaries and reinsurance intermediaries are a part of the financial system (Article 5)

Chapter XI Insurance Entities

Establishes the general guidelines of the insurance activity and social object

Chapter XII Insurance Intermediaries (brokers and agents)

Defines the type of insurances brokerage societies, its control and conditions for the exercise. It also refers to the activity of the agents.

Chapter XIII Reinsurance Intermediaries (brokers)

Defines type of society and social object, minimal conditions of exercise (capital and guarantees)

Second Part "Intervention in the Financial and Insurance activities"

Single Chapter Establishes the intervention functions of the National Government as regards financial and insurance entities.

Third Part "Financial Institutions operations norms"

This part contains twenty one chapters and all of them are in one or another form linked with insurance.

Chapter I Constitution

Procedure that must be followed by insurance entities, insurance intermediaries (brokers, agencies and agents) and reinsurance brokers to be constituted as such (corporations or cooperatives)

Chapter II Merger of Financial Institutions or *Insurance Entities*

Chapter III Acquisitions (purchase) of Financial Entities and *Insurance Entities*

Chapter IV Conversion and split-off (division) of Financial Institutions and *Insurance Entities*

Chapter V Assets, Liabilities and Contracts' transference

Chapter VI Transference of Business Portfolio of Societies of Capitalization and *Insurance Entities*

Chapter VII Norms relative to previous Chapters

Minimal capital requirements, authority vested in Financial Superintendence and administrative aspects

Chapter VIII Direction, Administration and Control

Chapter IX Equity Requirements

- Establishes the amount of *Minimum Capital* of insurance companies and insurances agencies. (Art. 80, Nº 1 and 2). Also establishes the equity' changes

- Establishes the *Solvency Margin requirement* (Art.82, Nº 2,3,4 and 5)

- Establishes sanctions for non fulfillment (Art.83)

Chapter X Ownership

Chapter XI Opening of offices

- Authorization to open branches or agencies **(**Art 92)

- Network office use by means of the subscription of a contract. (Art. 93)

Chapter XII Opening of foreign reinsurers offices

- Authorization to establish foreign reinsurers offices. (Art. 94)

- Obligation to register in the "Foreign Reinsurers Register" and "Foreign Reinsures Brokers Register"

Chapter XIII Financial and Commercial Information

- Power of the Superintendence for issuing insurance accounting rules

- Power of the Superintendence for publicizing the financial, investment and solvency margin situation.

- Power of the Superintendence for requiring Insurance Agencies to have a technical and accounting organization (Art. 95, Nº2)

Chapter XIV Competition and Consumer Protection

- Promotes free competition
- Establishes the Ombudsman,
- Complaints procedures,
- Authorization of advertising programs.
- Protection to policyholders on conditions of the insurance policies and tariffs
- Protection of insurance free hiring,
- Prohibited practices.

Chapter XV Properties Insurance of entities supervised by the Superintendence

Chapter XVI Prevention of Criminal Activities

Chapter XVII Illegal exercise of financial and insurance activities

State authorization requirement to develop the insurance activity and prohibition of activity for other persons

Chapter XVIII Others Investments and Financial Institutions Operations

Chapter XIX Obligatory Investment

Chapter XX Rescue Institutes and Protection of the Public Confidence

Chapter XXI Possession (intervention) by the Superintendence of the goods, money and business of the entity

Sixth Part "Conditions of the Capitalization activity and insurance companies, reinsurances and Insurance intermediaries operations"

This part contains seven chapters and all of them are linked with insurances.

Chapter I Aspects relative to the capitalization activity (includes some aspects of the insurance activity) Article 182 also refers to the insurers' investments. Indicates in what type of instruments the technical reserves must be invested.

Chapter II Special Norms relative to Insurance Companies

- Authorizes Operations related to Ceded and Assumed Reinsurance; and Pension Fund Administrators of Retirement and Disability (Art. 183)

- Policies and tariff system related to models and requirements (Art. 184)

- Special conditions of insurance contract (Art. 185)

- Systems of Technical Reserves and Investments (Art.186 y 187)

- Prohibition of commission's payment**.** It is only allowed to pay intermediation commissions to broker's societies, agencies or authorized agents. The commission payment or any other form of remuneration for intermediation work, to another person, is expressly prohibited **(**Art.188).

Chapter III Compulsory Insurances

Chapter IV Compulsory Personal Transit Accident Insurance

Chapter V Fund of Compulsory Personal Transit Accident Insurance

Chapter VI Special Insurances

Define the characteristics of some insurance (Profit sharing insurance, Life insurance for Public Ministry employees, Surety Bond, Currencies insurance, and Export Credit insurance)

Chapter VII Insurance Intermediaries

Norms relative to:

- Right of the Superintendence to grant or to deny the inscription of the insurance brokers

- Faculty of the Superintendence to examine at any time the knowledge of the persons that direct the "brokers societies" or "managers societies" that represent "insurances companies" (Art. 206)

- Commissions, the forms of payment and other conditions must be agreed between the agent and the companies.(Art 207, Nº2)

- Deficient exercise of the intermediary activity and violation of the legal and regulatory norms of insurances will give place to suspension of the "society broker", of the "agency" or of the "responsible agent". The loss of the right to obtain the renewal of the same one. (Art 207).

Seventh Part "Sanction System: System applicable to the insurance companies and to the directors, managers, legal representatives, and fiscal ticket inspectors or other officials of the companies**"**

This part contains four chapters and all of them are linked with insurance.

Chapter I General Rules (Art. 208)

Chapter II Sanction system to Persons (Art. 209 and 210)

Chapter III Sanction system to Institutions (Art 211)

Chapter IV Interests on Sanctions (Art. 212)

Eleventh Part “Procedure for the possession and Liquidation of the entities submitted to control of the Financial Superintendence”

This part contains three chapters and all of them are linked with insurances.

Chapter I   Possession and obligatory administrative Liquidation

Chapter II Possession

Chapter III Obligatory Administrative Liquidation procedure.

Twelfth Part “Procedure for selling of States’ shares in Financial Institutions and Insurance Entities”

This part contains three chapters and all of them are linked with insurances.

Chapter I   State participation

Chapter II Procedure

Chapter III Transitory dispositions.

Thirteenth Part “Inspection and overseeing authorities”

This part contains two chapters and all of them are linked with insurances.

Chapter I Guarantees Fund of Financial Institutions

Chapter II Financial Superintendence.

Appendix 9: Meeting List

Governmental Sector

Organization	Position	Person
1. Ministerio de Hacienda	Ministro de Hacienda	Dr. Oscar Iván Zuluaga
	Vice - Ministro	Dr. Juan Pablo Zárate
	Asesora del Director de Regulación	Dra. Marta Duran
2. Superintendencia Financiera	Superintendente Financiero	Sr. Augusto Acosta Torres
	Superintendente Adjunto	Sr. Rafael Eduardo Neira
	Superintendente Delegado para Aseguradoras e Intermediarios de Seguros y Reaseguros	Sra. Lucía Villate y su equipo técnico (legal, financiero y actuarial)
3. Departamento Nacional de Planeación	Director General	Dra. Carolina Rentería
	Director de Desarrollo Empresarial	Sr. Orlando Gracia
		Luz Estela Rodríguez y Mariana Sarasti
4. Bancoldex	Coordinadora – Banca de las Oportunidades	Dra. María Clara Hoyos

Insurance Private Sector

Organization	Position	Person
1. Federación de Aseguradoras Colombianas (Fasecolda)	Presidente Ejecutivo	Dr. Roberto Junguito
	Directora de Asuntos Internacionales	Sra. Rebeca Herrera
	Investigador de Estudios Económicos	Sr. Juan Manuel Restrepo
	Abogada Vicepresidencia Jurídica	Ana María Rojas
	Director Cámara de Vida y Personas	Juan Felipe Restrepo
2. Banco Caja Social	Vicepresidente de Mercadeo Estratégico	Sr. José Fernando Durán
	Gerente Líneas Microempresas	Sandra Moncada
3.Confederación de Cooperativas de Colombia (Confecoop)	Secretario General	Sr. Fernando A. Portilla
4.Oportunidad Latinoamérica Colombia	Director Ejecutivo	Sr. Fernando A. Alvira

5. Corporación Mundial de la Mujer Colombia	Gerente General	Sra. María Mercedes Gómez
	Gerente de Mercadeo	Sra. María del Pilar Velázquez
6. Marulanda Consultores Ltda.	Gerente General Consultora TSG Consultora	Sra. Beatriz Marulanda Sra. Lizbeth Fajury Sra. Mariana Paredes
7. La Equidad	Vicepresidente de Mercadeo y Ventas	Sr. Carlos Augusto Villa
8. Aseguradora Solidaria	Gerente Nacional Sector Solidario	Sra. Mónica Arroyave
9. Aseguradora Colseguros	Vicepresidente de Seguros	Sra. María Yolanda Ardila
	Gerente Customer Focus	Sr. Jorge Enrique Uribe
10. Mapfre	Sr. Germán Ariza	Gerente de Canales Alternativos
11. Liberty	Sr. José Raúl Moreno Sr. César Núñez Sr. Jorge Meneses	Gerente Nacional Affinity Secretario General Director de Gobierno Corporativo
12. Suramericana	Sr. Jhon Martín Mejía (entrevista escrita)	Gerente Suscriptor Vida Grupo
13. Corredores de Seguros Centro Seguros	Sra. Carolina Uribe	Gerente Comercial

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