

Discussion Paper: Micro-Insurance Regulation in South Africa
Comments by the South African Insurance Association (SAIA)

First draft

The SAIA has considered the proposals included in the National Treasury Discussion Paper on the Future of Micro-insurance in South Africa and welcomes the opportunity to submit the comments of our industry for consideration by National Treasury.

Introduction and background :

Pages 12 - 15

As stated in the Introduction and Background, as well as in the Executive Summary of this Discussion Paper, the paper seeks to propose that a regulatory space for the provision of micro-insurance products be carved out within the broader regulation of insurance provision in South Africa.

Micro-insurance, as per the definition accepted by the International Association of Insurance Supervisors (IAIS), is insurance that is accessed by or accessible to the low-income population, provided by a variety of different providers and managed in accordance with generally accepted insurance practices.

Because of the inherent complexity of insurance products, as well as the vulnerability of this market, it is essential that a balance is found between the protection of the consumers of this product type and the need to develop the market.

Micro-insurance is an internationally identified focus area, and South Africa with its clear objectives in terms of poverty alleviation, Black Economic Empowerment including the need to promote access and encourage SME development, as well as consumer protection should certainly be in the forefront of this.

Comments

Micro-insurance is identified internationally and locally as an important focus area. It is clear that a need exists for affordable and appropriate insurance products to the low income market. In order to facilitate the provision and distribution of such products, an enabling environment is needed. In principle, a regulatory framework that could facilitate this objective is welcomed.

A micro-insurance regulatory framework is also important in view of the fact that micro-insurance should be seen as a wider and more holistic area than just the Financial Sector Charter (FSC) related access space that currently exists in South Africa. From a consumer point of view (demand side), the need to alleviate risks will remain forever. And from the supply side, while it is true that the FSC Access space has encouraged South African insurance companies to enter the micro-insurance space, this might not be enough to address the needs of the low income market. In fact, if one considers CK

Prahalad's view that there is a fortune at the bottom of the pyramid, the insurance industry is in favour of creating an enabling environment.

The short-term industry is in favour of an environment that would make it easier to successfully serve the low income market, and assist them in meeting their FSC requirements. The short-term insurers experience a particularly difficult environment in terms of the cost of bringing appropriate products to a market that has limited or no experience of short term products. One of the big issues is the cost of distribution – see our comments on distribution later in this document.

Current reality: South African market

Pages 25 - 27

(Refer to Section 3.2 in the Discussion Paper)

The current reality with regards to the insurance market in South Africa includes the fact that South Africa has a relatively well developed insurance sector, with a substantial (in comparison to other countries) formal micro-insurance sector.

(3.2.1, 3.2.2)

However, this micro-insurance sector has several unique characteristics including the fact that the micro-insurance sector (formal) mainly consists of funeral insurance. Activity is increasingly taking place in the micro-insurance market as all companies operating in the financial sector are compelled by the Financial Sector Charter to become involved in the low income market. It is noted that the lack of an enabling environment impedes this progress.

Comment

One of the biggest stumbling blocks in this regard is the current regulation with regards to the distribution of products. Although the FAIS Act allows for a set of lower requirements for Category A intermediaries (assistance business which forms part of the micro-insurance market) other classes of business in this market should be allowed to benefit from such lower intermediation requirements in order to lower the cost of distribution.

It is also not in the interest of the micro-insurance market that micro-insurance products could be sold to this market using a completely non-advice model where there is no effective disclosure or access to information. The non-advice model is currently mainly used to distribute micro-insurance products in order to keep costs affordable with the ultimate aim of keeping the products affordable – although it has only been successful for funeral insurance. However, the experience in the market is that some form of advice or information giving is needed in order to distribute these products more successfully. An environment that would encourage a level of advice or rather information appropriate to a lower risk product would assist with both increasing access and achieving consumer protection.

(3.2.1 continues)

Comment [J1]: Tick box has been sold with great success in the funeral market

In the current SA reality, it is quite clear that a level playing field does not exist. Several unregulated and informal entities are operating in the micro-insurance market, and especially in the funeral market.

Comment

With traditional insurers having to comply with stringent prudential and other regulations, and the cost of compliance quite high, it would be advantageous if the better managed providers operating outside of the law brought could be brought within the regulatory net which would allow the regulator to clamp down on the abusive ‘fly by nights’.

However, this would only be equitable if there was a level playing field for conventional insurers. One would not like to exchange one un-level playing field with another so we would welcome the paper which appears to have this as its focus.

(3.2.4) Take-up

It is clear that take up of micro-insurance products in South Africa mainly relates to funeral business, and to a significant extent informal funeral type products.

Comment

An enabling environment is needed for other micro-insurance products, including short-term insurance products.

Definition of micro-insurance (Section 4)

Pages 33 - 35

The Discussion Paper seeks to limit the risk of the products while still allowing for the key needs of the micro-insurance market.

***Comment* ????**

This approach is supported. With a low risk product covering risk only, over a short term, meeting simplified standards, and having low benefit levels the prudential risk will be much lower allowing for lower compliance requirements and costs.

Comment [J2]: Think need to rework this para...

Benefit levels (4.2)

Page 37

The paper recommends a maximum benefit level of R50 000 per individual risk per year.

Comment 1

Although the idea of low benefit amounts is supported, the R50 000 cap might need to be reconsidered.

The current highest amount covered under the Mzansi short-term insurance access standards is R180 000, and although it is not suggested that this should be the limit, the maximum benefit level should be reconsidered, based on actuarial evidence, and in relation to the level of risk.

More information on a benefit levels will be provided after an actuarial exercise had been done.

Comment 2

It is suggested that a maximum benefit level is set per risk event and class of business. It is not accepted that the same maximum benefit level could be set for the different classes of business as each of these relate to different levels and values/sizes of risk.

Examples of why the current proposed cap might be problematic include the fact that a client could take out funeral cover for him, his spouse, three children as well as an extended family member which would very quickly add up to a bigger amount. In addition, it is a fact that the South African Government has been giving the title deeds to people who have been occupying council houses for a period and that the replacement value of these houses in terms of a homeowners policy if a total loss is experienced, for example, could far exceed R50 000 although the occupants could typically be in the micro-insurance target market.

Commission (4.2) ?

Page ?

The Paper suggests that commission on micro-insurance is uncapped similar to the current situation with funeral insurance.

Comment 1

In view of the fact that some level of advice/information giving, linked to the lower risk of the product, would be advantageous to a consumer who might not have high literacy levels as well as experience with these types of products, especially short-term insurance products, it might be a good idea to allow for higher commissions provided enough competition exists to keep commissions in check and there is effective disclosure.

The short-term insurance industry therefore supports this proposal.

It is proposed that commission should be paid on an ‘as and when basis’

Comment 2

As the commission would be on an as and when basis, it is likely that there will be a greater link to the continued provision of advice/information, which is to be supported. However, it is proposed that a potential hybrid model, i.e. a combination of up front and as and when commission should be considered in order to make it more likely and/or easier for intermediaries to be able to enter this market and make a living in the micro-insurance sector. As it is more likely that entry level intermediaries will enter this entry level market, it might be difficult and/or unattractive for appropriate persons to enter this market as intermediaries if only as and when commission is payable.

New act vs changing existing laws? (Section 5)

Pages 39 – 61

It is proposed that a new act is needed to create a new enabling regulatory space.

Comment

The SAIA is agnostic to whether a new act is needed or changes to existing legislation would be a better idea. The industry's view is that the focus should rather be on the elements the legislation to enable a micro insurance environment should include than on the debate between whether or not a new act is needed. The following is however relevant to this debate:

Pro new act:

In view of the fact that changes to many different existing acts would be needed to create this space, it might be a good idea to write and enact a dedicated act. Amending several existing acts (including the Short-term Insurance Act, the Long-term Insurance Act, the Friendly Societies Act, the Co-operatives Act, as well as the FAIS Act) might be less clear and more time consuming than to create a separate act. It might also be impossible to co-ordinate the amendment of all these acts to coincide in such a way that the new space is created as needed.

Pro amending existing legislation:

It is possible that amendments to the existing relevant acts, i.e. the Long- and Short-term Insurance Acts, as well as the FAIS Act should be sufficient to create an enabling micro-insurance space. It might be easier, and quicker, as some of this could be dealt with in terms of changing regulations rather than legislation itself.

In addition, holders of a 'full license' might not need a different act in this space, as an additional business class could suffice and the requirements of the Financial Sector Charter in terms of Access could be deemed enough of an incentive, especially after the gazeting of the Charter should this go ahead as intended.

The utility of the Co-operatives Act and the Friendly Societies Act should be investigated further with a view to amending them to assist in creating an enabling micro-insurance environment for smaller and new entities, as it is not envisaged that many such entities would apply for micro-insurance licenses in any event.

Facilitating intermediation and consumer protection (Section 6) Pages 66 - 75

Although a simplified product with limited cover, risk only, and short-term risk products, etc. will be the result of the proposed new micro-insurance framework, consumer protection is crucial. The first step towards consumer protection is to assist consumers in this market (as in every other market) to become informed consumers. Consumer education, information and advice should therefore go hand in hand with the distribution of micro-insurance products.

The FSC approach of including consumer education in the access requirements of the Charter is to be applauded and should in some way also be followed by the proposed framework.

In order for an enabling environment to exist for micro-insurance, in terms of consumer protection, the following are encouraged:

- Incentivising the giving of appropriate information of some sort through, for example, commission levels linked to advice/information given.
- Linking consumer education to access products. For example, all insurers may be required to hold a workshop on the product in a central location once a month which any policyholder could attend.
- Creating the space for an effective recourse system through a comprehensive consumer recourse plan.
- To provide effective consumer redress it is important that the current proliferation of avenues of consumer redress is minimised. This is necessary for two reasons: to minimise the confusion to consumers with the existence of a number of ombudsman offices with potentially conflicting jurisdictions and to prevent 'forum shopping'. We do not suggest a micro-insurance ombudsman but instead we suggest modifying (and where necessary fortifying) the current ambit and powers of the relevant ombudsman offices.
- Given the market segment at which the micro-insurance product is aimed, consumer redress must take into account the likely low levels of literacy and numeracy, and the limited access to current systems, e.g. the current requirement that complaints must be in writing.
- It is suggested that a central call centre with regards to relevant information in the micro-insurance space is established, with appropriate facilities such as toll-free numbers, sms, please call me and other more accessible communication methods.

(6.4)

The proposed regulatory framework for consumer protection is supported in its entirety, taking into account the above mentioned issues.

(6.5)

The SAIA and its members agree that any regulatory framework will fail should it not be effectively monitored, supervised and enforced.

The industry therefore supports 6.5 in this regard but questions whether the Regulator has the capacity to do so. In order to create this capacity, the cost of such additional capacity could become so onerous as to contradict the goal of creating an environment in which

the cost of doing business could be lower in order to facilitate the provision and distribution of appropriate and affordable micro-insurance products.

The cost of consumer education undertaken by the Regulator, and the way in which funds would be sought for this, should also be considered in more detail.

Potential gaps

(1.2) Scope of the discussion paper

The exclusion of certain indemnity health insurance products, as well as savings products, might be seen as a gap. Although it is noted that personal accident and disability products are included, it might be advantageous to include other health products such as hospital cash plans etc, as short-term insurance products related to assets (such as homeowners and household contents) are known to be very low on people in the lower income groups' priority lists. The latter product type might be more viable as group based products, including disaster risk insurance cover for vulnerable communities.

Current reality: International arena

(Section 9)

Comment

From the above, it is believed that it would be logical to include both prudential and product category related distribution allowances in a new micro-insurance regulatory framework that would encourage market development while keeping in mind consumer protection. We therefore support this approach.

As South Africa is actually in the forefront of developments in the micro-insurance space, it is not easy to find international examples that are relevant as is. However, the distribution allowances made in India and the prudential and operational allowances in place in the Philippines serve as good models, with some changes, and if combined could provide the most optimum environment for micro-insurance in South Africa.

Comment: Indian example

- Regulation allowing for a new type of intermediary, i.e. micro-insurance agent/intermediary, is seen as a desirable situation.
- It is not agreed that such agents/intermediaries should not be commercial or individual entities, but only NGOs, micro-finance institutions and community self-help groups. Although such groups could become intermediaries in this space, it should be possible to drive intermediation of micro-insurance products on a commercial basis.
- Micro-insurance should be encouraged as a potential profit driven enterprise in order to create a financially viable and sustainable model.

- The quota system in India is not supported as this could lead to consumer abuse and a lack of real commitment in this space. Albeit it is noted that South Africa has a quasi quota system in place as part of the FSC Access requirements.
- The fact that micro-insurance agents in real terms are earning higher commission is supported to encourage the optimal distribution of products together with an appropriate level of advise/information giving.

Comment: UK

It is agreed that a move towards product-based (or business class based) intermediation regulation could have its advantages in the micro-insurance space.

Comment: Philippines

It is agreed that a prudential and operational environment where a reduced regulatory burden and lower capital requirements are applicable to entities in the micro-insurance space, and/or micro-insurance as a product or business class, would be beneficial.

Comment: What can we learn from the micro-insurance experience in these two countries?

The team agrees with the lessons learnt from the limited international experience available, and agrees that “the best of both” approach should be followed.

3.4 In closing

In closing, it is reiterated that the Micro-Insurance General team believes that the proposed regulatory framework for micro-insurance should be supported, especially against a background of a need to increase access to people in the lower income group and to create an enabling environment for this goal to become a reachable one by the suppliers of insurance products.

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