

Promoting innovation in an index based insurance world

An introduction to the IAIS (draft) Issues Paper on Index Based Insurances



Overview

1. Project Background, Scope and Structure
2. Key features of the paper
 1. Pilots and proportionality
 2. Micro, Meso and Macro schemes
 3. Legal certainty
 4. Measuring and communicating basis risk
 5. Security and Reinsurance
 6. Project Sponsors
3. Next steps



Project Background, Scope and Structure



Background to the paper

- Several approaches to act over years were not taken up in the work plan
 - Focused on Accounting treatment concerns, insurance definition concerns
 - Case became stronger as market has continued to develop, and
 - Motivation for insurance supervisors is *consumer protection*.



The scope / target of the paper

- **Focus on areas that aim to improve the situation for low income people.** IAIS has been working on a range of “inclusive insurance” issues since 2006. The longest of any of the Standard Setting Bodies.
- **A more inclusive insurance market.** Discusses micro, meso and macro schemes so aims at an insurance market that better serves the underserved (directly or indirectly)
- **It is usually weather or other catastrophe risks related to agriculture or to natural catastrophe resilience. It can be other indexes. BUT excluding mortality and investment index products (largely for convenience).**
 - Some comments suggested focusing on one or other particular type of index (for example, index based crop insurance) but this was not considered to be necessary.
- **Project Sponsors** are a defined group in the paper – people who are part of the team bringing the project to fruition including insurers but also other parties involved.



Outline

- Introduction
- Background
 - Some definitions, and some guidance on stakeholders
- Supervision and Regulation
 - Formality
 - Insurable interest
- Consumer protection
 - Including products, basis risk, ex-gratia payments, subsidies, competition, and security of promises
- Pilots and proportionality
 - The ultimate goal defined
 - Proportionality for those not yet at the ultimate goal



Key Features

Pilots and Proportionality

Global Index
Insurance Facility



DAKAR2017
Global Index Insurance Conference

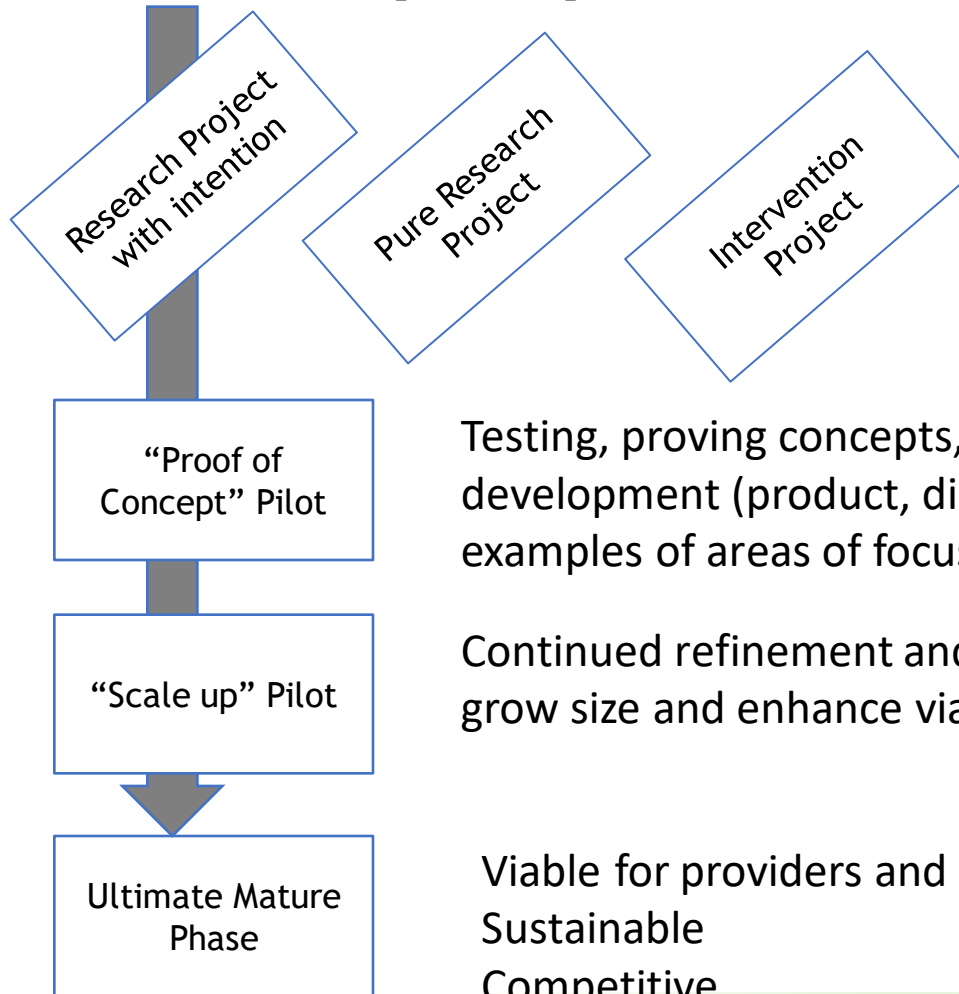


From the ideal world to the real world

- In the index based insurance area, there is a far greater preponderance of pilot projects.



Pilots and proportionality



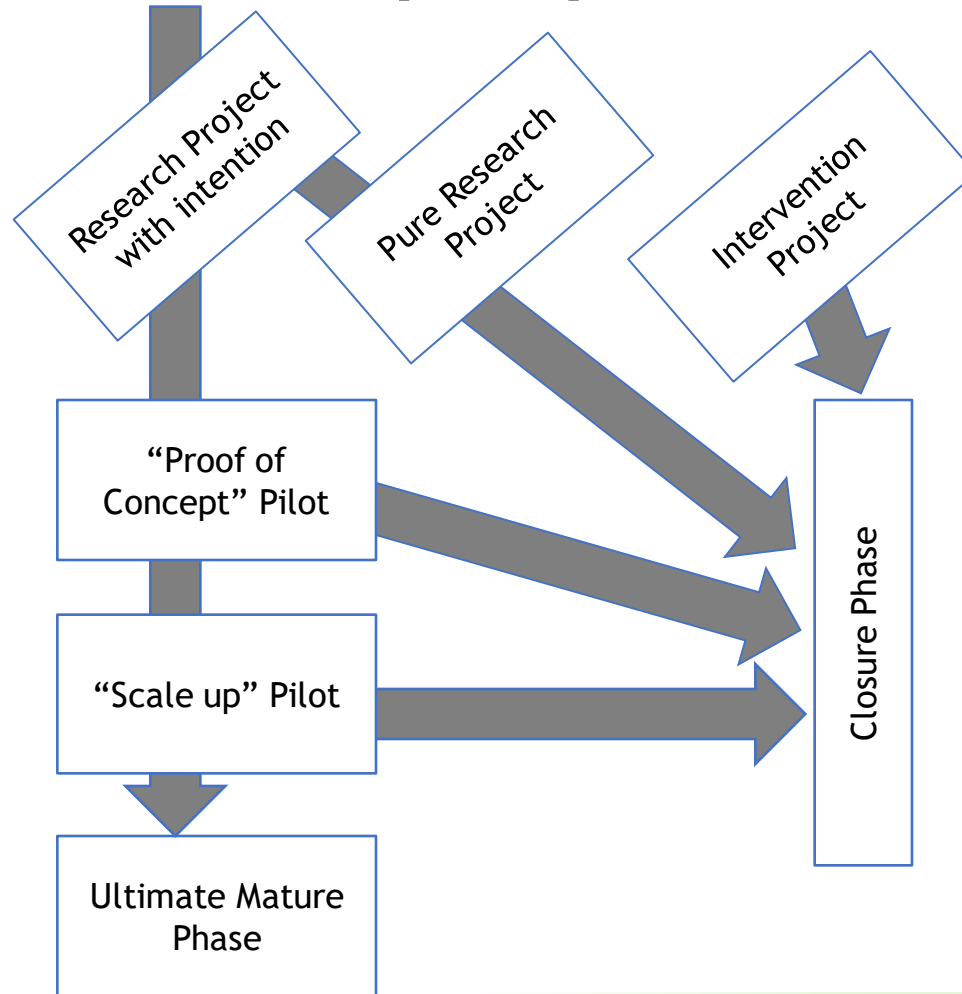
Testing, proving concepts, refining, adding different elements to the development (product, distribution, enhancing trust, education etc are examples of areas of focus at different times)

Continued refinement and improvements to delivery in an effort to grow size and enhance viability

Viable for providers and clients
Sustainable
Competitive
Without problematic subsidies
Formal, proportionately regulated and supervised



Pilots and proportionality



Project not continuing

Clients and operations have to be closed out effectively.

- Any ongoing liabilities under insurance have to be considered.
- Any outstanding service delivery issues?
- Withdrawal of service for those that had taken it up might be an issue.



Key Features

Micro, Meso and Macro Level Schemes



Defining Micro, meso and macro allows different approaches



- Our definitions might not be your definitions:
- Micro involves small policies for individuals or group schemes where individuals get coverage.
- Meso insures the meso entity and they communicate to members about their insurance of the meso entity but not insurance for individuals directly. No guarantee that things flow to one or other member of the meso organization.
- Macro is sovereign covers, and no communication of individual policy linkage from government to public.



Key items identified in the paper

- Making it clear that macro and meso are not micro
- Meso – relief in disclosure and consumer education by ensuring micro level clients are not considered to be insurance clients
- Macro – relief from most requirements is usual but some reporting is encouraged



Key Features

Legal certainty



Challenges to legal certainty

- Is it insurance or a derivative?
- Outcome: Product is included in the insurance supervisory framework
- Regardless of whether or not it is insurance for taxation or accounting purposes in the jurisdiction.
- If it looks like a duck it probably is a duck – what do people reasonably think it is? Particularly relevant for micro clients if they think they have insurance. How do the TCF and such approaches apply? It is not acceptable not to have consumer protection and complaint handling and fairly treated customers. Why duplicate it? For supervisors this is not only about the index based product but also for the implications for the insurance market as a whole. Product sponsors should not (some do by their actions) advocate that their product should be carved out and that the rest of the insurance market is not their concern. (Remember the Philippines case of education funding insurance)



Paper advocates that

- Index based insurances should be included under the scope of insurance supervision.
- Regardless of the treatment for other purposes.
- Insurable interest should not be a cause of this issue. The paper advocates a solution.
- Issuance by an insurer is important but can be varied under proportionality for macro schemes
- During pilots, licensing and formality can have proportionate solutions.

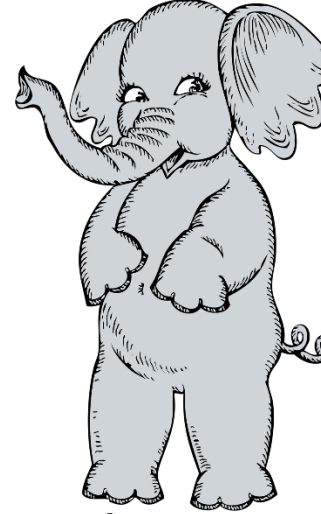


Key Features

Measuring and Communicating Basis Risk



Measuring & communicating basis risk



- Whilst basis risk is an issue with index-based insurance the paper makes the following observations:
 1. Not all problems that happen are basis risk problems even though it can be blamed for it.
 1. In fact, many of the reasons projects fail are nothing to do with basis risk.
 2. Attributing failure incorrectly to basis risk is a problem to be avoided.
 2. Not all basis risk events are the same – adverse basis risk is worse for policyholders than perverse basis risk
 3. Not all clients are the same – micro clients are less able to withstand an adverse basis risk event than others
 4. Communication is important by product sponsors
 1. Be open with clients that basis risk is a possibility
 2. Use back testing results to illustrate products
 3. Stochastic modelling might be useful for more sophisticated clients
 4. Share information with the insurance supervisor



Key Features

Security and Reinsurance

Global Index
Insurance Facility



DAKAR2017
Global Index Insurance Conference



During Pilot Stages

- Need to have the risk taking capacity. Can be through
- Capital
- Reinsurance
- Full asset support from a reliable source



Key Features

Project sponsors and supervisors



For Project sponsors

- Some guidance for Project Sponsors and Supervisors to help encourage communication at an early stage
- Annex provides concrete summary for project sponsors of some particular considerations



Next steps



NEXT STEPS

1. December 2017 and January 2018: Public Consultation at twice standard length of time
 1. Consultation comments should be submitted through IAIS on-line system.
 2. Closing date is not flexible for this final consultation round.
2. February 2018: Review and update paper
3. March 2018: Paper progresses through various committees to be adopted



Thank you!

Craig Thorburn
cthornburn@worldbank.org

