INSURANCE REGULATORY AUTHORITY

THE KENYA MICROINSURANCE POLICY PAPER

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EXECUTIVE SUMMARY

The Microinsurance Policy Paper maps out the future path for the regulation and supervision of microinsurance businessin Kenya. It spells out the objectives and key elements underlying this process.

In so doing, the paper makes policy recommendations that lay the foundations for the drafting of a legal and regulatory framework aimed at enabling the microinsurance market to develop in a sound and customer-oriented environment.

Microinsurance is an emerging trend in the Kenyan market and as such its regulation is not provided for in the existing Insurance Law. It is provided by a variety of institutions, and should be delivered in a way appropriate to low-income households with the products being designed as commercial insurance products that are fully funded by the premiums paid.

Microinsurance should be managed by insurers and other providers in accordance with generally accepted insurance principles and practices as it forms part of the broader insurance market. However, it is distinguished by its focus on the low-income sector, which has a number of repercussions for the way that it is provided and accessed.

The policy framework contained in this paper empowers the Authority to determine if an insurance product is a microinsurance product. However, it sets out strict criteria which the Authority will use when approving a product. These criteria will require the market to develop products that offer affordable premiums, uses easily understood contracts, has few exclusions, uses appropriate delivery channels and provides fast and efficient claims settlement.

The framework recommends creating a microinsurance company licence. This licence will require lower regulatory requirements than conventional insurance licences. It also recommends creating a microinsurance agent category that does not need to be licenced by the Authority and has lower training requirements. Both the company and agent will only be able to sell approved microinsurance products. Their creation aims to lower the cost of selling microinsurance products and increase the accessibility and customer value of insurance in the Kenyan market

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ABBREVIATIONS

AKI	Association of Kenyan Insurers
AML/CFT	Anti-Money Laundering/ Combating the Financing of Terrorism
CBK	Central Bank of Kenya
Cenfri	The Centre for Financial Regulation and Inclusion
CMA	Capital Markets Authority
CPI	Consumer Price Index
IAIS	International Association of Insurance Supervisors
ICT	Information and Communications Technology
ILO	International Labour Organization
IRA	Insurance Regulatory Authority
IT	Information Technology
MFI	Micro Finance Institution
MI	Microinsurance
NGO	Non-Government Organisation
RBA	Retirement Benefits Authority
SACCO	Savings and Credit Co-operatives
SASRA	SACCO Societies Regulatory Authority
SLA	Service Level Agreement
SMS	Short Message Service

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1.0 PURPOSE OF THE PAPER

This policy paper sets the framework for the development of microinsurance in Kenya. It also describes the background of the Kenyan insurance market and summarises the demand side, supply side and regulatory environment. This must be understood in order to set the best framework for microinsurance in Kenya.

Recently, stakeholders from the public and private sectors in Kenya have begun to include microinsurance in their agendas. This is because microinsurance is a key component to social and economic well-being and therefore has the potential to deliver an important pro low-income financial service. This is particularly so when used together with microfinance services savings and lending services and cashless payment systems. An increasing number of private insurers and intermediaries are pioneering the provision of microinsurance products in an environment that is lacking a policy framework to guide the development of microinsurance.

The government recognises the importance of providing an appropriate legal and regulatory framework for microinsurance. Therefore, the policy framework recommended by this paper is a key driver in the process of pushing the microinsurance agenda forward whilst at the same time integrating microinsurance into the mainstream insurance sector.

The paper proposes a policy framework that will be used to integrate microinsurance into the wider legal and regulatory framework for insurance. By means of specific provisions, the framework seeks to encourage and facilitate the provision and uptake of low cost, but high value insurance products that are appropriate to the needs of low-income consumers of insurance and that will enable them to effectively manage their risks.

The proposed policyframework for microinsurance is to be incorporated through the drafting of a new Insurance Act and Regulations.

2.0 BACKGROUND ON MICROINSURANCE

The need for enhanced access to insurance at affordable rates to the lower end of the marketis well set out in the Kenya Vision 2030 and other government policy documents. Compared to some other countries in Africa, the microinsurancemarket in Kenya is still under developed, although insurers are increasingly becoming active whileinformal “insurers” are expanding into the formal insurance system.

With access to insurance especially micro insurance being limited, Kenya like many other developing countries has identified microinsurance as key enabler for enhancing financial inclusion and mitigating risks.

2.1 Status of microinsurance in Africa

Low-income households are vulnerable to risks, a fact that is widely recognized as one of key drivers of underdevelopment(International Microinsurance Conference, Nigeria, 2013). In Africa, a continent with many infectious diseases, limited infrastructure, largely agrarian populations and fragile economies, low-income people are exposed to a multitude of risks that keep them in a vicious cycle of poverty.

Illness, death, natural disasters, damage to and loss of property, and accidents all have devastating effects on livelihoods especially in situations where there is no buffer to help people mitigate the financial impact of these events.

As opposed to developed countries, Africancountries do not have the financial means to provide the necessary government safety nets to successfully mitigate significant portions of their risks. Failure of informal schemes and government-led programs to address the population’s risk management needs opens a significant window of opportunity for microinsurance to mitigate low-income households’ vulnerability to risks and help smooth their way out of poverty.

In developing the regulations of and the market participation in this industry, policymakers and insurance supervisors in emerging markets and developing economies are increasingly becoming aware of the need to seek a healthy balance of regulation and enhancing access to quality insurance services while still protecting policyholders and other beneficiaries.

2.2 Kenyan microinsurance industry

A study by FinAccess conducted in 2009 revealed that therate of insurance penetration is below 3% of GDP, with only 7% of the Kenyan population having any form of insurance. It further revealed that the majority of the insured are drawn from the formal sector, which accounts for about 5% of the total population. This therefore means that majority of Kenyans in the informal sector is not adequately provided for by conventional insurance. A different concept of insurance is therefore necessary to facilitate the required growth by tapping into the potential existing in the informal sector.

Smallholder farmers, small traders and manufacturers and people generating livelihoods on a small and generally vulnerable scale constitute the base of the untapped microinsurance market in Kenya. Although the banking sector has been active in tapping into this market through micro finance institutions and savings societies, the insurance industry is yet to make a meaningful impact.

With this realisation,microinsurance remains a form of financial inclusion and access both of which are necessary preconditions for increasing insurance penetration. By givinginsurance access to the low-income and economically vulnerable households, the microinsurance agenda will support the Government's financial sector policy objectives as outlined in the Vision 2030.

3.0 CURRENT STATUS OF MICROINSURANCE

The microinsurance market features can be analysed from different points of view. This section gives a brief summary of the three main aspects influencing the microinsurance market – the demand for microinsurance from the public, the supply for microinsurance from insurance companies and the regulatory environment of microinsurance. This will help inform us what is currently prohibiting the development of the microinsurance market and therefore what policy changes are needed to encourage its future growth.

3.1 Demand Side

The features of the low-income and currently uninsured market were captured in the findings of the 2009 FinAccess survey. Subsequently, the Centre for Financial Regulation and Inclusion (Cenfri - A. Smith, et al, 2011) analysed the low-income market's experience of risk, as well as their perceptions of and demand for insurance products. Their key findings are summarised below.

3.1.1 Risk experience

According to the FinAccess report of 2009 loss of main wage-earner, followed by drought and/or famine have been underlined as major risks. Sickness, accidents and loss of property are also enlisted as major risks

These different risks imply different levels of impact and financial implications which, in turn, determine the type of coping mechanism used. The risk coping strategy mentioned most frequently by respondents is relying on the support of family members (25%). Other risk coping strategies include using savings (12.7%) and taking out a loan (10%). Less than 1% of adults say they would cope with a financial risk by claiming from insurance.

3.1.2 Perception of Insurance

A study carried out by Cenfri identifies several factors as contributing to the current state of perception of insurance and low penetration of insurance services especially among the low end market:

i) Lack of trust in insurance companies – this is characterized by non-payment of claims or lengthy and tiresome processes before a claim is paid.
ii) Low engagement and low awareness of insurance companies – the informal market is largely oblivious of insurance and regards the same as a preserve of the rich.
iii) Low understanding and lack of relevant insurance products – most of the information in the market is incomplete and of little value in helping the

customer to make valuable risk management decisions. There is also a pronounced lack of appropriate products for the low-income market.

iv) Some cultural and religious beliefs discourage people from taking insurance covers.

v) The government has not adequately supported insurance uptake by allowing tax exemptions and providing supporting fiscal measures.

3.1.3 Claims experience

Poor claims settlement has created a negative perception of insurance hence the slow uptake. The main causes of poor claims settlement are:

a) Mis-selling: clients are not aware of what is covered or not;
b) Inefficient claims settlement processes; and
c) Poor and inconsistent claims monitoring.

3.2 Supply Side

The key issues that are currently influencing the supply of microinsurance are the following:

i) Underwriters lack the necessary capacity to develop products, underwrite the products and processthe claims necessary to accommodate the unique features of this market.
ii) Insurance companies are struggling to keep the transaction and administrative cost low, while the current commission caps makes it hard to incentivise agents to sell the products.
iii) The bulk of thepotential market for microinsurance employed in the informal sector with staggered incomes that therefore cannot sustain consistent premium payments.
iv) Generally there is a poor perception of insurance, high insurance illiteracy levels and a poor understanding of products by the low-income segment of the population.
v) There exist informal risk mitigation mechanisms which makes low-income households hesitant to embrace insurance as a suitable risk transfer measure.
vi) There is a lack of adequatehistorical data to enable insurers and reinsurers to have a clear understanding of the risk exposure, which would assist them in proper underwriting.
vii) There is a lack of reliable IT solutions to facilitate successful potential real time transmission of information and cost effective operational processes to manage large volumes of small policies. These improvements should cut across the entire business line and value chain from new business sales to claims settlement.

3.3 Regulatory Environment

The regulatory scheme for microinsurance in Kenya, which includes all legislation impacting on the delivery of insurance, includes a number of Acts and their Regulations beyond the Insurance Act. The Banking Act, the Microfinance Act, the Co-operative Societies Act and the Savings and Credit Co-operative Societies Act all form part of the regulatory scheme and help determine the larger regulatory environment for microinsurance.

This policy paper gives recommendations of how to integrate microinsurance into the new Insurance Act and Regulations. The following summary discusses the obstacles to the development of microinsurance in Kenya caused by the current Insurance Act and Regulations. These should be address in the policy framework. They include:

a) Microinsurance is classified as a separate class of insurance business in the Act. Piecemeal amendments have been done over the years including defining microinsurance and separating microinsurance as a stand-alone class of insurance business. Nonetheless, challenges in the regulation of microinsurance still persist owing to the fact that factors affecting the business are qualitative rather than quantitative. The current legal framework still does not conform to international practices with regard to development of microinsurance, as set out in the IAIS Application Paper on Regulation and Supervision supporting Inclusive Insurance Markets.

b) Regulatory hurdles affecting the development of microinsurance products include:

    i) Capitalization levels, management and reporting requirements.
    ii) Stringent licensing requirements for agents and brokers, and restrictions on the amount of commission and management expenses.
    iii) Stringent definitions of what type of person or organisation is allowed to underwrite or sell insurance products.
    iv) Inability to bundle products and comprehensively address all the policyholder's needs.
    v) The need to get approval for the product design before launching the product and filepremium rates on an annual basis. This creates uncertainty over whether a product will be approved as microinsurance.
    vi) There is no model for sharing the costs and profits with distributors due to regulatory restrictions; hence mass aggregators see little potential in terms of revenues from microinsurance.

4.0 OBJECTIVES OF THE PAPER

The policy paper aims at achieving the following objectives:

4.1 Broad objective

Providing a framework for entrenching microinsurance as a tool for socio-economic empowerment and risk management for low-income households in Kenya.

4.2 Specific objectives

i) Encourage private sector engagement in risk protection for the low-income segment, and the development of a microinsurance market that is sustainable, sells products that meet the needs of the consumers and motivates consumers to buy insurance. (MARKET DEVELOPMENT)

ii) Relax barriers to entry and minimise the regulatory burden on underwriting and intermediation of microinsurance. This should promote competition amongst providers by ensuring a level playing field for big and small players where they seek to serve the same market. (APPROPRIATE REGULATION)

iii) Ensure sufficient prudential regulation and reporting. This requires tailoring regulation for the distinctive risks posed by microinsurance products and for microinsurance specific reporting requirements of financial and management information. (APPROPRIATE REGULATION)

iv) Facilitate the transition to formalised insurance provision by currently unlicensed providers. In the process, promote the formation of regulated and well-capitalised insurance providers, thereby supporting the development of small businesses. (FORMALISATION OF THE INDUSTRY)

v) Protect the interests of customers by requiring transparency with respect to product offering and servicing and by requiring insurers and intermediaries to treat their customers fairly. (CONSUMER PROTECTION)

vi) Ensure that customers understand and can easily comply with the claims process requirements and that the providers' process and pay claims quickly. (SOUND CLAIMS MANAGEMENT)

vii) Ensure the protection of the rights and privileges of the low-income insured and the prompt reaction upon complaints by requiring the creation of a defined customer complaint mechanism. (CUSTOMER COMPLAINT MANAGEMENT)

viii) Require the ongoing training of underwriters and distributers. Support effective financial literacy to improve the understanding of insurance and its associated risks and benefits forthe targeted customers of microinsurance.(CUSTOMER AND MARKET EDUCATION)

4.3 Scope of the Framework

This policy framework covers the provision of microinsurance necessary to enable the private sector to address the risk protection needs of low-income households. The policy framework does not set out any regulations. However, it does give recommendations on the type and nature of the insurance products and institutions the Insurance Act and Regulations should enable in order to achieve the objectives set out above.

5.0 POLICY FRAMEWORK

Any specific microinsurance regulation requires definitions of the products and institutions in order to distinguish it from other insurance products and institutions that are subject to a different set of regulation.

By having a separate definition, the Authority will be able to facilitate the development of a dynamic microinsurance industry by lowering regulatory burdens and barriers of entry and giving specified incentives for existing and new players to enter the market.

This policy framework consists of seven sections, which will cover the following:

- Section 1 gives the definition that will be used by the Authority to approve a product as a microinsurance product.
- Section 2 defines the type of institutions that the Authority will allow to underwrite and sell microinsurance products.
- Section 3 sets out the consumer protection requirements that microinsurance underwriters and agents will have to follow.
- Section 4 explains the prudential regulations that should apply to microinsurers.
- Section 5 discusses the tax benefits needed for microinsurance companies.
- Section 6 covers the consumer education programs that the Authority should initiate.
- Section 7 explains the transition arrangement that will apply to current formal and informal underwriters and distributors who want to transition to the microinsurance license.

5.1 Setting a microinsurance product definition

For the purposes of this paper, microinsurance is defined as insurance that has been designed to be accessible to the low-income population and where the risk insured under a microinsurance policy is managed based on insurance principles and funded by premiums. However, in order to facilitate the regulation of microinsurance, a stricter definition of a microinsurance product is given.

The definition of a microinsurance product is based on the following principles:

- The Authority and the insurance companies must have legal certainty on whether an insurance product is a microinsurance product or not;

- The definition should allow for the creation of dedicated microinsurers, although all insurers should be eligible to transact microinsurance business;

- The quantitative and qualitative elements should be set at the highest possible level to ensure the defined product is as inclusive as possible; and
- The quantitative and qualitative elements need toalign the resultingbusiness profiles with the expected proportionate regulation and supervision.

Having considered these principles and the need to align the definition to them, microinsurance productsaredefined generically, rather than as a list of specific product types.

The definition considers the characteristics of the product and industry that suggest separate regulation in the first place. The definition also seeks to avoid encroaching on or distorting other insurance markets. Therefore, it is written in a manner that limits incentives for regulatory arbitrage.

Giventhat the income level of the policyholder is hard to prove and makes the regulation of the product difficult, microinsurancewill not be defined by the income level of the population.

The definition will generate sufficiently low prudential risk to ensure microinsurance products can safely be provided by a wide range of microinsurers and be straightforward to distribute. This will allow for simplified regulatory and supervisory requirements.

5.1.1 Definition of a Microinsurance product

In order to ensure legal certainty over whether an insurance product is a microinsurance product, a product shouldonly bedefined as a microinsurance product if it is approved as one through the Authority's product approval process.

This policy framework sets out quantitative and qualitative criteria which the Authority will use to assess whether a product is indeed a microinsurance product. These criteria will give insurers developing new products the necessary clarity and certainty to proceed with their work.

5.1.2 Definition of a Microinsurance Actuary

In order to reduce the costs involved in developing microinsurance products and in running a microinsurance company, a new qualification for a "microinsurance actuary" needs to be defined.

The microinsurance actuary does not need to be a Fellow of the Actuarial Society of Kenya or have a recognized equivalent qualification. The appropriate lower level of qualification will be specified in the Regulations and guidelines to be issued by the Authority.When determining the requirements to qualify as a microinsurance actuary, the Authority should consult with and take into account any qualification standardsapproved by the Actuarial Society of Kenya.

The person qualified as a microinsurance actuary will be allowed to act in the capacity of a statutory or appointed actuary, if the company in question is a microinsurance company or if the product in question is a microinsurance product.

5.1.3 Product approval

Under the new framework, certainty over whether a product is a microinsurance product comes from the Authority's product approval process. Once a product has been approved by the Authority as a microinsurance product, the product is considered for all purposes of the Act and Regulations as microinsurance.

This will give the Authority the ability to protect customers and prohibit regulatory arbitrage by not approving products that are not deemed to be microinsurance products.

The Authority may revoke its approval at any time if it considers that the contract no longer satisfies the criteria for microinsurance. In that case, the insurance contract ceases to be regarded as microinsurance from the date of the revocation or such later date as may be specified in the revocation notice. A revocation notice does not affect the status of the contract as microinsurance before that time.

In applying for product approval, the insurance or microinsurance company must:

- Submit all new microinsurance products to the Authority for review before launching the products. The Authority will aim to give approval within 10 working days of receiving all the necessary documentation.

- Include the proposed policy documentation as well as a summary of policy features including the risk events covered, exclusions, benefits level, premium (with sign-off on pricing), the commission and fee structure and the claims documentation and processes.

- Include details on the sales process and the key service providers. Copies of the service level agreements with the key service providers must be provided.

The company can only proceed with the launch once the Authority gives its approval.

In addition to the initial application, the insurance companies should submit annual reports to the Authority on the performance of the product, for at least three years, using templates issued by the Authority. This information will form part of the ongoing product monitoring process, as explained in section 5.1.5.5.

Any significant changes to the product design relating to these criteria should be reported to the Authority. The insurer must receive approval of the changes before they can be implemented in the market. The Authority may update these criteria through the updating of the relevant microinsurance Regulations.

5.1.4 Microinsurance approval criteria

The product design must meet the following criteria in order for the Authority to approve it as a microinsurance product.

5.1.4.1 Nature of the product

In order to be a microinsurance product, the product must conform to the requirements of generally accepted insurance practices (which should include the Insurance Core Principles).

Schemes that do not provide contractually guaranteed benefits such as social welfare and emergency assistance by governments fall outside the definition of microinsurance.

5.1.4.2 Cover type

It is proposed that the microinsurance product category include only risk benefits with no surrender value. Risk benefits provide cover against a certain risk event or a combination of risk events, as defined in the policy contract, with the occurrence of the risk event serving as a trigger for a claim. No savings component may be included. Licencedmicroinsurers will therefore not be able to write endowment policies, nor policies with a cash-back component.

A consequence of this restriction is that microinsurancepolicies must disclose how many claims and the monetary limit thereof may be made within the contract period.

This requirement is necessary to justify the reduced prudential and market conduct regulation required from microinsurance companies. This requirement can be reviewed over time as the risk management processes of microinsurance products improves.

Non-insurance companies, for example banks or other regulated savings institutions, can provide saving products that can be bundled together with microinsurance risk products.

5.1.4.3 Sum assured

All Microinsurance policy benefits should be defined on a first loss or sum assured basis. First loss insurance refers to insurance that provides a defined benefit upon a defined event as opposed to indemnity insurance that indemnifies losses, i.e. pays benefits according to the actual value of the loss suffered.

The maximum sum assured under a micro insurance policy should be capped at anappropriate level.The cap applied will be different for different product classes to reflect the need to limit the risk profile of these products while ensuring the cover meets the needs of the low-income households.

Given that the maximum amounts will almost certainly need to be revised, it is important to retain flexibility. Therefore, the actual monetary values would be better placed in guidance issued by the Authority, rather than in the regulations, which will take longer to amend, and the regulations should provide for this.

The following provisions will apply to the maximum sum assured:

- Where more than one person is insured under a single individual policy (for example a family cover product), the cap applicableshouldbe adjusted accordingly.

- Where the product underwrites policyholders on a group basis, the sum assured cap should apply to the average sum assured of thelives insured under that single policy.

- Benefit limits should be reviewed at least once every three years, taking account of the CPI published by the Kenya Bureau of Statistics and industry developments.

Insurers will be permitted to structure policies to allow claims to be paid in instalments if this was provided for in the contract. For example, a micro-insurance policy may pay 30% as a lump sum to address the risk event with the balance being paid monthly as a form of income replacement. However, the claims process and communication with the client should be finalised within 10 working days, as set out in section 5.1.5.3.

5.1.4.4 Maximum contract term

The policy contract duration has a significant impact on the underwriting risk of a particular product with longer term policies being more risky than short-term policies.

It is proposed that microinsurance policies have a contract term of up to but not exceeding 12 months. The premium must be fixed at the start of the contract and not be changed for the period of the cover.

To facilitate uninterrupted cover, microinsurance policies can be renewed at the end of the contract term without the need for a new policy document.The only provision is that the policyholder continues to pay the premium.

5.1.4.5 Waiting periods

The standard waiting periods that apply to conventional insurance products also apply to microinsurance products, except in the following situations:

- A waiting period of up to 9 months is allowed for maternity health benefits. A waiting period of up to 6 months should be allowed for elective surgery.However, the waiting period is restricted to a maximum of two months for other benefits on health microinsurance products.

- The waiting periods in microinsurance policies should be restricted to a maximum of two months for benefits on death or disability due to natural causes.

- The waiting periods should be restricted to a maximum of one month on non-life microinsurance products or in the case of accidental deaths.

- If a policyholder voluntarily decides to join a group insurance scheme, then the waiting period that applies to the member should be restricted to a maximum of one month. However, if it is compulsory for a policyholder to join a group insurance scheme, then no waiting period is allowed to apply to the member.

- No waiting period shall apply on the renewal of an existing product.

5.1.4.6 Exclusions

Microinsurance must have very few exclusions. This helps the policyholder understand their policy and gain trust in insurance. It makes the claims process easier and lowers the chance of claim rejections, which again increases trust in insurance.

The policies can have exclusions for pre-existing conditions or any other risk the insurer deems necessary. However, a policy must:

- Only have exclusions that the policyholder is aware of when applying for the policy; and

- Describe all exclusions within the policy summary document.

During the product approval process, the insurer must provide a justification for the use of any exclusion.

5.1.4.7 Grace period

The policy will only be activated once the first premium is paid by the client.

To ensure that the policyholder is not unduly disadvantaged by their irregular cash flow, a grace period of twice the premium payment frequency starting on the premium due date shall apply, but limited to a maximum of two months. This will apply after each premium instalment. If a policyholder submits a claim during the grace period, the value of the claim may be reduced by the sum of the unpaid premium(s).

However, the grace period requirement will not apply to index-based microinsurance policies.

5.1.4.8 Policy documentation

To ensure that the policyholder understands the product prior to purchase and knows how to pay premiums and make claims, the policy documentation must meet the following requirements:

- **Policy Wording:** Microinsurance policies must be simple and easy to understand and policy documentation must be provided in plain language, avoid uncertainty or confusion, should not be misleading and contain minimal legal and technical terms.

  The documentation must be prepared in EnglishorKiswahili.The intermediary must offer the documentation to the customer in either of the two languages.

- **Policy Summary**: Before the product is sold, the customer must be given a simple policy summary, whether electronic or otherwise, of no more than two A4 pages with a minimum font size of 10, covering the following:
  - Name of the insurer and address of its principle office in Kenya;
  - What are the sum assured and benefits and a description of risks insured and any exclusions or limitations that applies;
  - What disclosure obligations there are from the policyholder before buying the contract and the implication of the policyholder giving a self-declaration that he/she is in good health;
  - Where and how doesthe policyholder pay the premiums and the consequence of non-payment?
  - When the cover starts and what waiting periods apply, the duration of the contract and how it will be renewed;
  - When, where and how the policyholder can claim and what documents will be required?
  - How to contact the insurance company and provide the customer care contact number;
  - The right and method to make a complaint; and
  - Where and how the policy can receive a copy of the full policy terms and conditions.

- **Policy terms and conditions**: The full policyterms and conditionsmust be made available to the policyholder.The document, whether electronic or otherwise, may also not be more than two A4 pages. However, smaller font sizes may be used as long as it can still be clearly read.

- **Benefit payment documentation:** When a benefit is paid or rejected, the explanation of the reason and how the benefit amount was calculated must also be clearly and in simple terms documented and explained by the insurer to the claimant.

  In the case of the benefit being paid during the grace period and the benefit being reduced for unpaid premiums, this must also be explained.

5.1.4.9 Premium basis

Insurers providing microinsurance products should be able to underwrite policies in the manner they consider most appropriate.There should be no prescribed or minimum premium basis or limits on what is seen as an "acceptable return" on the microinsurance policy.

5.1.4.10 Microinsurance actuary premium sign-off

The insurance company must secure sign-off on the total premium (and not only the risk premium) for all new microinsurance products, as well as any changes in the pricing, by a microinsurance actuary. The sign-off on the total premium should allow for scrutiny regarding the proper allocation of expenses, loss ratios as well as allow for profit and investment income.

5.1.5 Microinsurance approval guidelines

In designing the product, the insurer must take into account the following attributes and make certain they are within the guidelines provided by the Authority.

The Authority will consider the justification for the design choices when deciding whether to give approval as a microinsurance product or not. The approval can be revoked if the Authority finds that the product is not meeting these attributes.

The Authority will give the exact guidelines for the submission and approval of a microinsurance product.

5.1.5.1 Premium payment frequency

In order to facilitate the payment of premiums by the low-income target population of the microinsurance product, policyholders will be allowed to pay the premiums of the annual policy on a daily, weekly, monthly or any less frequent basis.

5.1.5.2 Changing the premium, non-renewal

Should the insurer no longer find the level of risk acceptable, it may decline to renew the policies or increase the premiums, with a minimum ofone month's notice provided to the policyholders in either case.

The insurance company will need to submit the premium rates on a file-and-use-basis to the Authority, with a justification for any significant changes. The premium rates can be revised at any point during the year for new policies sold or for policies being renewed during the year.

The new premium rates needs to be submitted to the Authority two months prior to the new premium rates taking effect. The company does not have to wait for regulatory approval and can start using the new premium unless the Authority objects to the rates.

5.1.5.3 Policy Administration

- The insurance company or intermediary must issue the main policyholder with some kind of proof of payment, be it in printed or electronic format, as soon as a premium payment has been made.In the case of a group policy, only the master policyholder needs to receive a receipt.

- The main policyholder must receive confirmation that he or she is a new policyholder within 10 working days of signing up for the insurance policy. This communication should also remind the policyholder of the main terms and conditions of the insurance cover.

- Once the policy is activated, the insurance company or intermediary must issue the main policyholder with the following **policy issue information**:
    - insurer's name;
    - customer care contact number;
    - policy number; and the
    - policyholder's name.

  The above information may be provided to the policyholder within the policy documentation, on a separate document or using ICT methods.

- **Policy renewal**: If the policy is to be renewed, the insurance company must notify the policyholder that the last premium of the current policy term has been paid and that the next contract term will automatically start with the next premium payment.

  The insurance company must provide this notice one month in advance of the renewal date. Such notice shall clearly state the renewal premiums and benefits of the policy.

- **Claims payments**: All valid microinsurance claims payments should be made within 10 working days of the receipt of the required documentation. Alternatively, the reason for the rejection must be given if not valid with details of who to complain to.

  After the insurance company has made the payment, the claim payments must be confirmed to the policyholder with some kind of receipt, be it in printed or electronic format.

- **Claims Documentation:** Insurers should minimize the burden (on both consumers and delivery channels) of making claims by streamlining processes and requiring minimal documentation. For example, in order to claim a death benefit, the required documentation could be limited to a death certificate and some form of identification of the deceased and beneficiary.

  The exact claims documentation requirements will be specified in the guidance notes provided by the Authority.

5.1.5.4 Use of ICT

The potential of ICT application in microinsurance could range from clients registration, premium collection & administration and claims management to client servicing and payment among others. To fully embrace the potential of ICT, the regulations should allow for:

- Providing marketing and sales information using ICT. Therefore, the ICT should be allowed to replace the need for an agent to sell microinsurance products.However, the information provided must meet the same requirements as for microinsurance agents, as explained in section 5.3.2.

- The submission of the required documentation for applying for microinsurance and making claims through electronic means.

- The collection of digital signatures or Kenyan PIN numbers on mobile phones (or similar ICT method) to serve as client confirmations, to the extent possible under the exiting AML/CFT regime.

- Replacing the policy summary with a SMS (or similar ICT method) that contains the same information as required above. For the policy documentation and terms and conditions, the insurance company may instead refer the policyholder to a website or mobile website (mobisite), if they are certain the policyholder has access to the internet.

- Issuing the policy issue informationusinga SMS (or similar ICT method). The equivalent information required in section 5.1.5.3 must be clearly shown.

- Notice of premium changes, policy cancellations and policy renewal to also be given using a SMS (or similar ICT method).

- The use of mobile systems for paying premiums, receiving information and receipts and receiving claim pay-outs etc. to the extent made possible by other acts and regulations that govern the use of mobile payment systems.

However, before the Authority will allow an insurance company to make use of any ICT, the company must be able to prove to the Authority that it meets the minimum hardware and software requirements necessary to support the ICT, or has a service level agreements in place with providers who do meet the requirements. The exact requirements will be specified in guidelines issued by the Authority in cooperation with the Kenyan Communications Authority.

5.1.5.5 Ongoing product monitoring

When deciding whether to continue giving approval for a product to be sold, the Authority should monitor the following product performance indicators on an annual basis as part of its supervisory process.

- **Incurred Claims ratios**

The Authority will issue criteria or guidance on the minimumincurred claims ratio– based on the gross earned premiums– that will be acceptable on microinsurance policies. This is to ensure that the product provides acceptable value to the policyholder

- **Aggregate Distribution costs**

The Authority will issue criteria or guidance on the maximum aggregate annual distribution costs - commission, fees, marketing and administrative costs – that will be acceptable on microinsurance policies.

- **Individual and average sum assured**

The Authority will monitor the individual and average sum assured of the policies sold. These must be below the level of the sum assured caps specified as part of section 5.1.4.3.

If the microinsurance company fails to meet the requirements of these product performance indicators, the Authority reserves the right insist that the company takes steps to address this or to revoke the approval of the sale of the policy.

5.1.6 Microinsurance product features

The following features are not required of microinsurance products. However, if they are included in the products, they should meet these requirements in order for the Authority to give approval as a microinsurance product or not.

5.1.6.1 Bundled products

The regulations should allow for the bundling of life and non-life products, I.e. one policy combines more than one type of cover. When bundling of different products occur:

- Only one insurance company may underwrite all the bundled products.
- The bundled products should consist of only microinsurance products and should not be bundled with conventional insurance products. However, microinsurance products should be allowed to be bundled with other non-insurance products i.e. microfinance loans.
- The sum assured caps will apply separately to the individual parts of the bundled product, and not to the combined total of the sum assured of all the parts of the product. However, individual products may not be repeatedly bundled together in order to increase the total sum assured cover provided by the policy.

- Only the combined premium payable by the policyholder has to be disclosed to the policyholder. However, the insurer must be able to calculate and report the premiums associated with each discrete element of cover separately.

5.1.6.2 Group cover

Insurers providing microinsurance products should be able to underwrite policies on an individual or group basis.

Where policies are underwritten on a group basis, insurers should not be able to selectively cancel (or refuse to renew) individual policies within the group. Should the insurer no longer find the level of risk acceptable, it must decline to renew the policies for the whole group or increase the premiums for the whole group, with a minimum of one months' notice provided to the policyholders in either case.

Where group underwriting is applied, no price discrimination will be allowed between individuals within a group other than on the basis of age at entry and level of cover.

Where the age profile of the group changes, the microinsurer may reprice for the group as a whole, but not for individual aging members.

In the case where the master policyholder in a group cover has the right to determine the pay-out made to the individual policyholders, the method or formula used by the master policyholder to calculate the pay-outs must also be submitted to the Authority.

5.1.6.3 Reinsurance

There should be no requirement to have a reinsurance treaty in place in order for a product to be approved as a microinsurance product. However, the microinsurance actuary must, in setting the premium, consider if the company can absorb all the risk from selling the product.

5.1.6.4 Cooling off period

The microinsurance product does not require a cooling off period. It will be up to the insurance company's discretion whether to include a cooling-off period or not.

5.1.6.5 Marketing material

All marketing material used by the insurance company must be simple and easy to understand and be provided in plain language, avoid uncertainty or confusion, should not be misleading and contain minimal legal and technical terms.

5.2 Licensingrequirements

5.2.1 Corporate structure of a licenced microinsurer

5.2.1.1 Formalisation

Inclusive insurance products and services should be provided within the provisions of the legal and regulatory framework. In particular, all entities that act as insurers should be subject to licensing.

Where informal services exist, formalisation will be needed. For instance, NGOs, SACCOs and MFIs offering insurance to their clients or members should either outsource the risk to a licenced insurance company or acquire a licence to operate an insurance company.

The transition requirements from an informal to a formal insurer are described in more detail in section 5.7.

In order to facilitate the formalisation process, and therefore increase the number of companies offering and underwriting microinsurance products, a separate insurance company licence should be created.

5.2.1.2 Microinsurance licence

A company that meets the minimum requirements to transact insurance business should be allowed to apply for a microinsurance licence. A company holding such a licence shall be restricted to providing only products that meet the definition of a microinsurance product.

However, in order to encourage and develop the microinsurance market, a microinsurance licence will have the following benefits over a conventional life or general insurance licence:

- The minimum regulatory capital requirements will be lower.
- The regulatory requirements for pricing contracts will be simplified and less prescribed.
- Will be able to sell both life and general microinsurance products and therefore allow for the bundling of products.
- Will be allowed to use a microinsurance actuary to act as the appointed or statutory actuary of the company.
- If the microinsurer is part of a group that includes licenced general or life insurance companies, the microinsurer will be allowed to use the

same management and company structures as the general or life insurance company.

- The transition requirements will make it easier for companies who want to change or formalise their business under a microinsurance licence.

The prudential requirements of microinsurance companies are discussed further in section 5.4.

5.2.1.3 Minimum requirements

Although solutions are available that can take account of the nature, scale and complexity of the entity and its risk profile, there is a minimum point below which it will not be possible to retain insurance risk. Therefore, companies that do not meet this minimum size will not be allowed to apply for a microinsurance licence or operate as a microinsurer.

The minimum size and requirements will reflect the need for:

- A microinsurer to be a corporation incorporated under the Companies Act.
- Risk pooling to exist. Therefore, the institution must already have access a sufficiently large membership base or show in its business plan how it will be able to attract a large membership base.
- Having effective business processes to manage retained risk.
- Having a realistic business plan showing how it will be able to sell microinsurance profitable.
- Meetingboth financial and management informationreporting requirements.
- Treating customers fairly.

In addition, insurance risk should not be carried on the balance sheet of entities that also do other financial or non-financial business. If entities are operating mixed businesses, they should separate the insurance business into a separate legal entity.

The minimum conditions for a microinsurance company licence will be specified in the relevant parts of theInsurance Act and Regulations.

5.2.1.4 Conventional insurance licenced companies

Companies that currently hold life or general insurance licences should also be allowed to sell both life and general microinsurance products without having to apply for a separate microinsurance licence. However, they will:

- Have to maintain the full requirements of their conventional licences.
- Be allowed to use the same management and company structures for both the conventional and microinsurance business.
- Have to comply with the separate reporting requirements for their microinsurance products as may be required by the Authority.
- Have to separate their conventional and microinsurance assets and policyholder liabilities and hold the microinsurance assets and policyholder liabilitiesin a separate microinsurance fund.
- Have to hold the minimum capital requirements for dedicated microinsurance companies in addition to their general or life insurance licence minimum capital requirements. Their risk-based capital requirements will reflect their additional microinsurance obligations.

The Authority will review this allowance in the future and may require insurance companies to apply for and meet the requirements of a separate microinsurance licence if they what to underwrite microinsurance products. However, the Authority will give sufficient notice to the industry if this becomes the requirement.

5.2.2 Microinsurance product distribution

5.2.2.1 Microinsurance agents

In order to facilitate the distribution of microinsurance products, a separate category of microinsurance agents shall be created who will only be allowed to sell approved microinsurance products.

The Authority will delegate the responsibility for the licencing of microinsurance agents to the licenced insurance companies or intermediaries. The licenced insurance companies or intermediaries will issue a license, supervise and collect performance information on all their microinsurance agents and report this information to the Authority from time to time. The Authority will then supervise the licensed institutions to ensure the individual microinsurance agents meet the specified requirements.

A microinsurance agent must meet the following standards:

- Undergo an approved microinsurance training program and pass a qualifying examination at the end of the program. The Authority shall approve the training programand qualifying exam of the microinsurance agents. The exam can be either a written or a practical examination. The total mandatory time necessary for the training and examination of microinsurance agents should be limited to25 hours.

- Abide by a prescribed code of conduct that details explicitly how sales should and should not be conducted.

- Pass a background check by the licenced institution to verify that they meet the fit and proper requirements set out by the Authority.

- Be issued with an identity card stating the name of the specified person, name of the employer and whether he or she is empowered to collect premiums.

All staff engaged in selling microinsurance should meet the requirements of microinsurance agents specified above.

Licenced insurance companies and intermediaries must appointat least one key individual who meets the requirements of a conventional insurance agent. The key individual will oversee the activities of the microinsurance agents.

Microinsurance agents should be prohibited from working with more than one life, general or microinsurance company.

In the case of individual agents, the payment of the premium and claims must be done directly between the insurance company and the policyholder and may not be done via the individual microinsurance agent's bank account. However, if the microinsurance agent works for a licenced insurance institution, the payments can be done via the institution's bank account.

Conventional agents and brokers shall be allowed to sell microinsurance products and services under their existing licences.

5.2.2.2 Aggregators

In order to act as an aggregator, an organization does not need to have an intermediary license.

The licenced insurance company must inform and receive approval from the Authority prior to commencing the sale of microinsurance products through the aggregator. Therefore, the service level agreement with the aggregator and the details of the branding arrangement and the product to be sold shall be submitted to the Authority for review and approval.

Where an aggregator is used, the following provisions apply:

- Only a legally registered entity will be allowed to act as an aggregator.
- Should the sales process rely on an aggregator regulated by a separate supervisory authority, a letter of approval or no objection may be required from that authority.
- The insurance companymust provide the training on the insurance products to the staff of the aggregator to enable them to act as microinsurance agents.
- Only the staff trained in a specific microinsurance product will be able to provide the information on that specific microinsurance product. The staff should receive the same level of training as the individual microinsurance agents.
- The aggregator must provide the same information to the customer as is required from a microinsurance agent.
- The responsibility to ensure no mis-selling takes place should rest with the insurance company that uses the aggregator.
- The aggregator can use a third party administrator to administer the premium collection, data collection and the claims payments.
- The payment of the premiums and claims can be done via the aggregator's bank account.
- The aggregators must inform the policyholder of the name of the insurance company backing the policy. The policyholder must always be made aware they are buying an insurancepolicy and be given the approved policy summary and documentation. The policyholder must

be informed of how they can contact the insurance company where they can lodge a complaint.

- In the case where the purchase of insurance is mandatory in order to purchase a product or service (for example to receive a loan), the aggregator must be able to disclosure to the policyholder the name of the insurer, the level of the cover and the value of the premium component of the total purchase price.

- The aggregators will be allowed to collaborate with multiple life and non-life companies to offer products best suited to their members. However, the staff will then have to be trained by the different insurance companies to understand how the different microinsurance products work.

5.2.2.3 Key distribution channels

To better reach underserved customers,aggregators can be any entity registered for purposes other than insurance and with an existing client base.

These could includebanks, retailers, microfinance institutions, post office branches, funeral homes, NGOs, cooperatives and SACCO’s, social and religious associationsand utility service providers (electricity, gas, telephone and mobile) among others.

5.2.3 Requirements of the Service Level Agreements

The service level agreements between the insurers and third parties will be reviewed by the Authority as part of their supervisory process. The insurer must be able to provide to the Authority on an annual basis a report on the actual level of service received from the service provider compared to the level specified in the agreement.

Permission to continue using the third party service provider or aggregator will depend whether the requirements of the agreement has been met to a satisfactory standard.

The minimum requirements of the service level agreement required by the Authority will be specified in guidance notes issued by the Authority. However, they should include the following:

- **Due diligence report**: The SLA should specify what due diligence was done before appointing or engaging an aggregator. The SLA must also address business rules prohibiting aggregators from transferring problems from one insurer to another without proper recourse and dispute resolution.

- **Define legal relationships and responsibilities:** The legal relationship and responsibilities of all parties involved in facilitating the provision of the product need to be mapped out in terms of the regulatory environment and oversight.

- **Penalties and fines:** The SLA should be clear in specifying dispute resolution, arbitration and who will be responsible for the paymentof penalties and fines. It should provide fora means by which the licenced insurance company can impose fines and penalties from the Authority onto the unlicensed aggregator or microinsurance agent.

  The Authorityshould enforce a clause to have the aggregator obtain a clearance certificate from the previous underwriter.

- **Turn-around time for claims settlement**:The SLA should capture details on the claims handing speed and process requirements, including the roles of each partner in the claims handling process.

- **Complaints handling**:The SLA should clarify how complaints by one party of the agreement with another party in the agreement should be handled.

- **Creating a living will:**The SLA should specify how, in the case of the failure of the arrangement, the insurer, aggregator and supervisor will ensure that:

  - a sufficient and well-communicated notice period is given;
  - alternative options are available to clients, including voluntary paid cover, before the scheme is stopped;
  - arrangements are made concerning appropriate payment mechanisms for the alternative schemes;
  - the aggregator and insurer continues to monitor and address complaints for a set period;
  - the supervisor is routinely updated on the wind down of the scheme and the levels of complaints.

The Authority should create an example Microinsurance SLA template for customization by the various Microinsurance operators, in order to assist companies in the creation of acceptable documents.

5.2.4 Commission and fees

5.2.4.1 Commission

Given the nature and expenses incurred in the distribution of microinsurance, the current levels of regulated commissions are not enough to cover costs for brokers and agents. Also, sharing commission with non-regulated bodies (intermediaries such as MFI's) is not allowed.However, microinsurance agents may be allowed to receive commission.

Restrictions on commissions should avoid creating a disincentive to provide services to the underserved segment of the population. Remuneration should also encourage effective servicing beyond the point of sale.

Therefore, the commission on microinsurance products should apply as follows**:**

- Microinsurance commissions must be capped at 25% per annum across the term of the policy.
- Commissions be payable as a fixed percentage of each premium paid to incentivize the service of policyholders post-sale.
- Aone-off policy initiation fee may be paid to the microinsurance agent, with a maximum of Kenyan Shillings 2,000.
- The regulations should allow for claw back arrangements between the underwriter and the intermediary in case of early lapses of the policy. The formula and maximum amounts should be specified in guidance issued by the Authority.

5.2.4.2 Salary, fees and profit share

- An aggregator that acts for a licensed insurance company can be remunerated in any form of either fees or profit-share basis. Payments may be structured as the insurance company and aggregator sees fit.

  The remuneration arrangements of the staff who work for the aggregator and sells the microinsurance shouldnot be subject to the same regulatory restrictions on commission and fees as applies to microinsurance agents. The regulatory restrictions will only apply to the arrangement between the insurance company and the aggregator.

- Microinsurance agents employed by an insurance company or intermediary may be remunerated in the form of a salary, commission, fee or a combination of these.

In all arrangements, the total amount paid must fall under the cap on total distribution costs.

5.2.5 Penalties and fines

The penalties and fines given to microinsurance agents and aggregators should be proportional to their size and value of the premiums transacted. Therefore, the penalties and fines imposed on microinsurance institutions and aggregators should be significantly larger than those imposed on individual microinsurance agents.

Microinsurance institutions should be responsible for enforcing the conduct of microinsurance agents and aggregators under their control.This should be addressed in the service level agreementbetween the licenced insurance company and the unlicensed aggregator or microinsurance agent.

5.3 Consumer protection requirements

5.3.1 Corporate Governance

All Microinsurers will be required to adhere to current good corporate governance requirements, including the need for transparency, integrity and skilled management. However, requirements should be reduced to take into account the lower prudential risk of microinsurance companies compared to conventional insurance companies.

If the microinsurer is part of a group that includes licenced general or life insurance companies, the microinsurer will be allowed to use the same management and company structures as the general or life insurance company.

5.3.2 Sales process and minimum information to provide

The following information has to be provided by the microinsurance intermediaries. They must explain the:

- The name and registration number of the agent;
- The information given in the policy summary, as set out in section5.1.4.8; and
- If the insurance was part of the purchase of other goods or services, what part of the payment is towards the insurance and if the insurance purchase is mandatory or not.

The agent must have access to a list of frequently asked questions and answers to give to the customer in case the above information is not sufficient for the customer.

The agent should collect all the data required to administer the policy.

The full policy documentation must be made available to the policyholder. This can be either given as part of the policy summary or using ICT, as explained earlier.

5.3.3 Know your client and Money laundering

To the extent possible under the exiting AML/CFT regime, the “know your client” and anti-money laundering requirements should be relaxed or eliminated recognizing the microinsurance context. Client verification through a photo-bearing ID or substitute document should be sufficient.

5.3.4 Group policies

The requirements for group policies should apply for both conventional and microinsurance. Where the conventional group insurance requirements in the new Insurance Act and Regulations do not address the needs of microinsurance group policies, the following requirements should apply.

In order to protect the individuals that are part of a group microinsurance product, the microinsurer must meet the following requirements:

- The insurer must issue a master copy to the group or person administrating the group. The insurer must also enter into a written service level agreement with the administrator setting out the terms of their arrangement.

- In addition, separate notification of the cover has to be given to each member of the group, informing them where to obtain more information on the policy.

- The individual policyholders will have the right to cancel their cover at any time, subject to any separate agreement that the policyholder may have with the group policyholder – for example as a requirement for taking out a loan. However, this requirement will not apply to index-based microinsurance policies.

5.3.5 Dispute resolution / Consumer care and recourse

The insurer must operate a telephone customer care service for the policyholder to contact with any questions concerning the microinsurance policy. The staff operating the contact point must be specifically trained for the microinsurance policies and for how to deal with microinsurance policyholders.

Every microinsurer shall also maintain a client care system through which clients can lodge complaints and receive redress.

Complaints involving microinsurance benefits shall be acted upon within 5 working days of filing a complaint, and a resolution shall be made within 1 month from the time the case is submitted for final resolution.

If the company does not compensate the client for his complaint, it must inform the client where and how to reach the Authority's consumer complaints department.

5.3.6 Microinsurance Policyholder Compensation Fund

Currently, there are two separate policyholder compensation funds being administered for life and general insurance companies. They are being funded by separate premium levies.

In order to protect the microinsurance policyholders and to ensure the premium levy on a microinsurance company is appropriate for their risk offailure and the amount they can afford, the Authority should assist in setting up a separate microinsurance policyholder compensation fund, funded by a separate premium levy on microinsurance companies.

5.4 Prudential regulations

The proposed criteria for microinsurance products will limit the prudential and market conduct risks of underwriting these products. This facilitates the creation of a prudential and market conduct regulatory framework tailored to lower risk products.

5.4.1 Capital requirements

The minimumcapital requirements of a dedicated microinsurance company will be the greater of the following amounts:

a) Kenyan Shillings 50 million.

   This amount will be reviewed at least once every three years, taking account of the CPI published by the Kenya Bureau of Statistics and industry developments.

b) The risk based capital requirements, as set out in the regulations. The risk based capital requirements for microinsurance risks will be different from conventional insurance and reflect the unique nature of microinsurance products and the microinsurance company.

A microinsurance company should not be required to hold any capital based on their net earned premiums of the preceding financial year.

The transition capital requirements for companies that formalise their insurance business are set out in section 5.7.

5.4.2 Reserving requirements

The reserving requirements for microinsurance products sold under a microinsurance licence will be the same as for products sold under a general insurance licence. This is a prudent requirement since both companies will issue contracts on a one year renewable basis. The reserving basis for a product sold under a general insurance license is given in the regulation.

The reserving requirements for microinsurance products sold under a life insurance licence will depend on the nature of the product sold.

- If the nature of the product sold is the same as that of a long term product sold under the life insurance licence, the company will have the option to use the reserving requirements as under a life insurance license.

- If the nature of the product sold is the same as that of a short term product, the reserving requirements will be the same that of products sold under a general insurance license.

5.4.3 Microinsurance Fund for conventional insurance companies

As specified in section 5.2.1.4, conventional insurance companies that areselling microinsurance will have to hold their microinsurance assets and corresponding microinsurance policyholder liabilities in a separate microinsurance fund.

5.4.4 Asset requirements

Licenced microinsurers will only sell contracts with terms that are limited to a maximum of one year. Therefore, it is proposed to apply an investment regime suited to short-term, liquid investments:

- Only cash (or liquid, cash-like) or Kenyan government bonds will be allowed as the assets backing the policyholder liabilities andthe minimumcapital requirements.

- If a microinsurer's assets exceed its reserving andminimum capital requirements, it may apply to the Authority to invest such free assets or a portion thereof in other asset classes.

These requirements will not apply to convention insurance companies who sell microinsurance business.

5.4.5 Management expenses

Specifying management expense requirements in detail dictates a particular balance between different parties in the value chain, which may not reflect the reality of microinsurance. Therefore, the basis for these assumptions will not be specified in the regulations.

5.4.6 Reinsurance

There is no actuarial reason for compulsory reinsurance. As long as pricing is signed off by the microinsurance actuary, reserving should be adequate and the risks accounted for. Therefore, it should not be compulsory for microinsurers to have any reinsurance.

However, we recommend that microinsurance companies put in place catastrophe reinsurance cover. This is especially needed for recently formed microinsurance companies who will have weak risk management processes in place and whose policyholders are more likely to be concentrated in one geographical area, making them more prone to insurance catastrophes.

5.4.7 Appointed actuary and statutory actuary

A microinsurance company will be allowed to appoint approved microinsurance actuaries to perform the functions of appointed actuary or statutory actuary.

5.4.8 Statutory returns and Data

A standard template will be developed for audited annual and unaudited quarterly statutory returns, taking into account the current returns for life and general insurance companies.

- Microinsurance companies will only have to submit the microinsurance template. Where products are bundled, the company must unbundle the results and report it separately under the appropriate product categories.

- The insurer will be required to submit information on all their distribution costs for monitoring by the Authority.

- Licensed conventional insurers should be able to write policies for all types of risk currently being written under the Insurance Act. However, where the product is categorised as a microinsurance product, the information on these products should be reported separately in the microinsurance templates.

The exact reporting requirements and templates will be specified in the regulations.

5.4.9 Statutory auditing

A microinsurer must appoint, and at all times have, one or more qualified external auditors to sign off on financial statements intended for submission to the Authority.

5.5 Tax

The tax regulations will not form part of the Insurance Act and Regulations and should be addressed elsewhere. However, it is recommended that a proposal for tax relief or incentives for all microinsurance programmes be made to the government.The proposal should:

- Ensure a level playing field between similar policies written by a life or general insurance company and those written by a microinsurance company.

- Allow for tax relief and incentives for providers and distributors of ICT, those undertaking research and development and areas of consumer education, awareness and any other outreach programs.

- Encourage companies to target the potential microinsurance clients that live in the counties, instead of only focussing on the clients living in cities.

5.6 Education

The Authority should be involved in the coordination of the efforts of government departments, insurance companies, intermediaries, NGOs and learning institutions on providing financial training to both the consumers and the providers of insurance.

5.6.1 Consumer Education

The Authority will coordinate with other financial service regulators, e.g. CBK, CMA, RBA and SASRA to improve national financial literacy.

The Authority will also coordinate with the different insurance companies and associations to develop a coherent consumer educationstrategy.Whilst it should be a requirement for insurers to play a role in financial education we recognise it may be difficult for companies to develop their own education strategies, primarily due to the high cost of developing and distributing materials.

Therefore, an alternative is to develop a joint program on behalf of the insurance industry to promote financial education, specifically targeting education about insurance and its role as a risk management tool. The program should be a countrywide multimedia program funded by all insurance companies, allowing for important economies of scale.

If the program is a joint effort of many insurers it will result no one product or company being promoted, but instead allow for all insurers to be treated equally.

Other options include the training of National Microinsurance champions and incorporation of insurance in the formal education curriculum. Insurers could also help though an adopt-a-school campaign and the introduction of Insurance clubs in schools.

5.6.2 Provider Education

The Authority will assist in encouraging the development of the actuarial and management skills of the providers of microinsurance. There will be a need for the running of seminars and workshops that shall focus on the insurance companies' responsibilities to clients, various prudential, market conduct and good governance requirements and on client rights and responsibilities

The Authorityshould also improve the industry's actuarial capacity by strengthening the linkages between the market and training institutions for graduates.

5.6.3 Actuarial Education

The Authority should assist the Actuarial Society of Kenya in developing a suitable qualification requirement for microinsurance actuaries. They should work together to develop a way to test and certify that someone is suitablyqualified to act as a microinsurance actuary. They should also develop opportunities for the microinsurance actuaries to participate in ongoing professional development training sessions.

5.6.4 Microinsurance agent training

In order to assist insurance companies with the training of their microinsurance agents, the Authorityshould develop a microinsurance agent training course. It should not be made mandatory for insurance companies to use this course to train their agents. However, it will assist small insurance companies who do not have the expertise to develop such a course on their own to meet the Authority's training requirement of microinsurance agents.

5.7 Transition requirements

In order to assist in the formalisation of the current informal underwriters, the Authority will allow for the following transition arrangements. The transition arrangements will also apply to current formal underwriters and intermediaries who want to apply for the microinsurance licence.

Formalisation should be clear, transparent, and based on transition plans that provide incentives to formalise and limit excessive risk taking before full transition.

The new regulations will not influence current licensed insurance companies, agents or brokerages whounderwrite or sell microinsurance, since the new regulations will not prohibit them from continuing to do so. Companies who are not currently transacting microinsurance and wish to do so will have to follow the normal application process specified in the Act and Regulations.

5.7.1 Application for Microinsurance Company Licence

To ensure a sound and orderly transition of all those entities currently providing microinsurance without a licence, it is proposed that the new Insurance Act and Regulations allow for a transitional period of three years from the date of the enactment of the new Act.

During this period:

i) All entities that currently provide insurance without a license must register as an insurer or terminate their insurance activities.

ii) The entities that want to continue as microinsurers will have 12 months from the enactment of the new Act to apply for a provisional microinsurance licence from the Authority. The provisional microinsurance license will require the company to have a minimum capital of Kenyan Shilling 25 million. They will also have to submit a business plan that explains how they will achieve the full license requirements at the end of the 3 year transition period.

iii) The entities that do not wish to apply for a full insurance licence must either obtain underwriting from another registered insurer, including a microinsurer, or stop selling their insurance policies and dispose of all their insurance obligations within the 12 month transition period.

iv) As soon as an entity applies for the provisional licence, it will become entitled to receive support from the Authority.The regulatory requirements for the rest of the three-year period will reflect their current informality and their desire to either obtain a full licence or end all their insurance business.

v) At the end of the 12 month period the option of obtaining a provisional licence will lapse.Those entities that do not apply for the provisional licence in the 12 month period will be subject to immediate prosecution under the proposed enforcement campaign.

vi) All entities that can meet the full compliance requirements, including the full minimum upfront capital requirement, may register as a full microinsurer and start operating as such at any time within the three year period.

vii) If after the end of the 3 year transition period they have not achieved the full licencing requirements of a microinsurer, the provisional licence will lapse. They will then have to follow the requirements of the Insurance Act and Regulations for all companies who fail to meet their licencing requirements, which may include arranging underwriting with a registered insurer or terminating their insurance activities.

5.7.2 Application for Microinsurance Intermediary Licence

To ensure a sound and orderly transition of all those entities currently acting as a microinsurance intermediary without a license, it is proposed that the new Insurance Act and Regulations allow for a transitional period of one year from the date of the enactment of the new Act. During this period:

i) All entities that currently distribute insurance without a license must register as an agent, aggregator or brokerage or terminate their insurance activities.

ii) The entities that want to continue as a microinsurance agent or aggregator will have one year from the enactment of the new Act to register with a licenced insurance company or intermediary. They may also register with companies who have obtained a provisional microinsurance licence.

iii) The transition period is intended to provide sufficient time to allow microinsurance agents to receive the necessary training and aggregators to reach an agreement with a licenced insurance company or intermediary and submit it to the Authority for approval.

iv) If after the end of the one year transition period they have not completed the necessary requirements of microinsurance agents or aggregators,they will be subject to immediate prosecution under the proposed enforcement campaign.

5.7.3 Approval of the current microinsurance products

Many insurance companies are currently selling “microinsurance” policies. These companies can continue selling their current “microinsurance” products until a determined transition date set in the regulation. They will have to report on these products as required in section 5.4.8.

However, if they want to continue making use of the regulatory benefits of having the product classified as a microinsurance product, they will have to adjust the product to meet the microinsurance requirements and submit for approval before the end of the transition date.

6.0 CONCLUSION

As noted in the situational analysis, the Kenyan insurance industry has mainly focused on corporate and property markets despite the majority of the Kenyan working population being in the informal sector. It is not surprising therefore that the rate of penetration into the insurance market is below 3% of GDP covering only about 7% of the population.

In the Insurance Act Cap 487, microinsurance is regulated under miscellaneous class of business. This means that microinsurance is regulated under the conventional insurance law which does not adequately provide for the insurance needs of the low-income households.

This policy paper summarizes the challenges faced in the design, distribution and administration of microinsurance products. It then makes policy recommendations concerning the creation of new regulatory definitions, institutions and requirements.

By incorporating these recommendations it is believed that the objectives of the policy paper will be achieved and that a regulatory environment will be created that will address the problems identified in the industry and facilitate the growth of microinsurance.

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